Supreme Court, U.S.
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Nos. 00-568 AND 00-809

In The

Supreme Court of the United States

People of the State of New York and the Public Service Commission of the State of New York, et al.
Petitioners,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

Enron Power Marketing, Inc.,
Petitioner,

v.

Federal Energy Regulatory Commission, et al.,
Respondents.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

JOINT APPENDIX (Vol. 1 of 2)

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NOTICE

The following documents have been omitted in the printing of this Appendix. These documents may be found in Petitioner Enron Power Marketing, Inc.'s Appendix to its Petition for Writ of Certiorari (00-809) at the following pages:

APPENDIX A:

Judgment of the United States Court of Appeals for the District of Colombia Circuit filed 6/30/00 . . . . . 1a

APPENDIX B:

Opinion of the United States Court of Appeals for the District of Columbia Circuit filed 6/30/00 . . . . . 3a

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Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, Notice of Proposed Rulemaking, [1988-1998 Proposed Regs.] F.E.R.C. Stats, & Regs. ¶32,514 (1995) (pertinent portion) 33,047-33,085 . . . . . 553a

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Some may also be found in the Petitioner's People of the State of New York and The Public Service Commission of the State of New York's Appendix to its Petition for Writ of Certiorari (00-568) at the following pages:

APPENDIX A:

Order of United States Court of Appeals for the District of Columbia Circuit filed 8/22/00 . . . . . A-1

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RELEVANT DOCKET ENTRIES IN DISTRICT OF COLUMBIA CIRCUIT

DOCKET FOR CASE NOS.: 00-568 and 00-809
(Court of Appeals Docket No.: 97-1715, Complex)

12/5/97	PETITION FOR REVIEW CASE docketed. Petition for Review filed by Petition Transm Access Plcy. [314268-1] (mcm) [97-1715]
1/2/98	CLERK'S ORDER filed granting non-party motion to intervene filed by VT Dept Pub Srvc [316424-1]. (sha) [97-1715]
1/12/98	CLERK'S ORDER filed granting non-party motion to intervene filed by Edison Elec Inst [320723-1] granting non-party motion to intervene filed by City & Cty San [320823-1] granting non-party motion to intervene filed by Oprt Co Amer elec [318537-1]. (mcm) [97-1715]
4/30/98	CLERK'S ORDER filed, on court's own motion, that cases are consolidated; FURTHER ORDERED that EEI motion for leave to amend is granted. The amended motions are dismissed as moot, in light of 1/12/98 order granting EEI leave to intervene in 97-1715; FURTHER ORDERED that motions of WA Util, So CA Gas, KS City, PSI Energy, and Cincinnati Gas to intervene be granted; FURTHER ORDERED that parties advise the court by 5/15/98 of any remaining motions, etc.; FURTHER ORDERED that petitioners show cause, by 6/01/98 why the

petitions for review in 98-1110, 98-1117, 98-1121, 98-1130, 98-1133, 98-1135, 98-1138, 98-1144, 98-1151, 98-1157, 98-1158, 98-1161, 98-1164, 98-1167, 98-1179 should not be dismissed as incurably premature. Responses limited to 20 pages and failure to respond will result in dismissal. Respondent may file a reply, limited to 10 pages, within 10 days thereafter; FURTHER ORDERED that by 6/01/98, parties shall provide a list of five lead counsel. Within 30 days thereafter, counsel shall provide joint proposed briefing schedule, etc.; FURTHER ORDERED that parties shall resubmit Rule 26.1 disclosure statements by 6/01/98, etc.; FURTHER ORDERED that respondent shall provide by 5/15/98 a current master service list; Clerk is directed to send a copy of this order by certified mail to petitioners in cases identified above. (su) [97-1715 98-1179 98-1180]

6/2/98 CLERK'S ORDER filed granting non-party motion to intervene filed by Suffolk Cty Elec [355394-1] granting non-party motion to intervene filed by Fl Pub Svc Cmsn [354722-1] granting non-party to intervene filed by Rochester Gas & Elec [354086-1] granting non-party motion to intervene filed by Carolina Power [353289-1] granting non-party motion to intervene filed by FL Power & Light [353301-1] granting non-party motion to intervene filed by Pub Svc Elec Gas [353314-1] granting non-party motion to intervene filed by OH Consum Coun, Natl Assn St Util [353328-1] granting non-party motion to

intervene filed by Dairyland Power Coop [353189-1] granting non-party motion to intervene filed by Natl Rural Elec Coop [353333-1] granting non-party motion to intervene filed by NE TX Elec Coop Inc, Sam Rayburn Elec G&T, TX-LA Elec Coop TX [352000-1] granting non-party motion to intervene filed by FL Muni Power Agcy [352033-1] granting non-party motion to intervene filed by MI S Ctrl Power Agcy [352034-1] granting non-party motion to intervene filed by Wolverine Power [352035-1] granting non-party motion to intervene filed by Pub Svc Cmsn St NY [352047-1] granting non-party motion to intervene filed by Natl Assn Reg Util [352050-1] granting non-party motion to intervene filed by NY St Elec & Gas [350758-1] granting non-party motion to intervene filed by GA Transm Corp [354045-1]. (mcm) [97-1715]

8/13/98 PER CURIAM ORDER: on the court's own motion, that these case be designated "COMPLEX". FURTHER ORDERED that the order to show cause be discharged. FURTHER ORDERED that the petitions for review in No. 98-1110, 98-1117, 98-1121, 98-1130, 98-1133, 98-1135, 98-1138, 98-1144, 98-1151, 98-1157, 98-1161, 98-1167 and 98-1179 be dismissed as incurably premature. [374127-1] FURTHER ORDERED that the initial briefing schedule is as follows (SEE ORDER FOR BRIEFING FORMATS) [374127-2]: Petitioner's brief due on 10/1/98 in 97-1715; Intervenor supprtng Petitioner's

brief due 10/1/98 in 97-1715; Respondent's brief due on 2/1/99 in 97-1715; Intervenor supportg Respondent's brief due 4/1/99 in 97-1715; Petitioner's reply brief due 5/3/99 in 97-1715; Intervenor supprt Petitioner's reply brief due 5/3/99 in 97-1715; Deferred appendix due on 6/10/99 in 97-1715; Final briefs due on 6/24/99 in 97-1715. FURTHER ORDERED that motion for leave to file joint proposed briefing schedule be granted. The Clerk is directed to file the lodged pleading [363672-1]. FURTHER ORDERED that the motion to exceed page limits be granted. FURTHER ORDERED that the motion to change party name be granted. The Clerk is directed to amend the docket to reflect that the intervenor's name is Enron Power Marketing, Inc. rather than the Coalition for a Competitive Elec Market [360864-1]. FURTHER ORDERED that the motion to intervene filed by IL Power Co [360901-1] be granted. FURTHER ORDERED that the motions adding a new attorney [356458-1] filed by 11 movants and Ontario Hydro [356721-1] be granted. Lead counsel are as follows: John Conway (FERC), Susan Court (FERC), Robert Zener, Robert Jablon, Jonathan Feinberg, Sara Schotland, Peter Kirby and Isaac Benkin (lead counsel for petitioners and intervenors). FURTHER ORDERED that the motion of Pacific Legal Fndtn for leave to participate as amicus [353194-1] and for leave to dispense with service on all parties be denied [353194-2]. This denial is without prejudice to PLF's refiling the motion for

leave within ten days of the date of this order, after serving all parties listed in the current master list. Before Judges Wald, Sentelle, Randolph. [97-1715] (mcm) [97-1715 98-1110 98-1117 98-1121 98-1130 98-1133 98-1135 98-1138 98-1144 98-1151 98-1157 98-1161 98-1167 98-1179]

8/13/98 PER ABOVE ORDER lodged motion establishing the initial briefing schedule [363672-1] is filed. (mcm) [97-1615]

10/1/98 BRIEF [DISCRIMINATORY DISCOUNTING AND FUNCTIONAL UNBUNDLING] filed by Petitioner Transm Access Plcy in 97-1715, Petitioner Transm Dpndnt Util in 98-1145, Petitioner Enron Power Mkt Inc in 98-1178 [386444-1]. Copies: 15. of service date 10/1/98. [97-1715, 98-1145, 98-1178] (mcm) [97-1715 98-1145 98-1178]

10/1/98 BRIEF [INVESTOR OWNED UTILITY PETITIONERS] filed by Investor IL Power Co in 97-1715, Petitioner Pub Svc Elec & Gas in 98-1119, Petitioner FL Power & Light in 98-1120, Petitioner Rochester Gas & Elec in 98-1124, Petitioner Carolina Power in 98-1125, Petitioner NE Util Svc Co in 98-1126, Petitioner NE Util Svc Co in 98-1127, Petitioner NY St Elec & Gas in 98-1139, Petitioner Boston Edison Co in 98-1162, Petitioner Ctrl VT Pub Svc Corp in 98-1162, Petitioner Niagra Mohawk Power in 98-1168, Petitioner Con Edison Co NY Inc in 98-1174,

Petitioner Con Edison Co NY Inc in 98-1175, Petitioner GPU Engy in 98-1176, Petitioner Edison Elec Inst in 98-1180 [386545-1]. Copies: 7. Certificate of service date 10/1/98. [97-1715, 98-1119, 98-1120, 98-1124, 98-1125, 98-1126, 98-1127, 98-1139, 98-1162, 98-1168, 98-1174, 97-1175, 98-1176, 98-1180] (mcm) [97-1715 98-1119 98-1120 98-1124 98-1125 98-1126 98-1127 98-1139 98-1162 98-1168 98-1174 98-1175 98-1176 98-1180]

10/2/98 BRIEF W/2 VOLUME APPENDIX OF LEGESLATIVE HISTORY [STATE COMMISSIONS] filed by Intervenor for Petitioner WA Util Trans Cmsn in 97-1715, Intervenor St NJ Bd Pub Util in 97-1715, Intervenor WY Pub Svc Cmsn in 97-1715, Intervenor for Petitioner ID Pub Util Cmsn in 97-1715, Intervenor for Petitioner NC Util Cmsn in 97-1715, Intervenor for Petitioner Natl Assn Reg Util in 97-1715, Intervenor for Petitioner FL Pub Svc Cmsn in 97-1715, Petitioner People St NY in 98-1111, Petitioner Pub Scv Cmsn St NY in 98-1111, Petitioner VA St Corp Cmsn in 98-1142, Petitioner AR Pub Svc Cmsn in Petitioner VT Dept Pub Srvc in 98-1148, Petitioner OH Coun in 98-1150, Petitioner Natl Assn St Util in 98-1155 [386734-1]. Copies: 7. Certificate of service date 10/1/98. [97-1715, 98-111, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155] (mcm) [97-1715 97-1111 98-1142 98-1147 98-1148 98-1150 98-1155]

2/16/99 BRIEF filed by Respondent FERC in 97-1715 [416562-1]. Copies: 6. Certificate of service date 2/16/99. (mcm) [97-1715]

4/16/99 BRIEF filed by Intervenor Edison Elec Inst in 97-1715, Intervenor NY St Elec & Gas in 97-1715, Intervenor Cm Edison Co in 97-1715, Intervenor Consum Engy Co in 97-1715, Intervenor VA Elec Power Co in 97-1715, Intervenor New Engl Power Co in 97-1715, Intervenor WI Pub Svc Corp in 97-1715, Intervenor Atl City Elec Co in 97-1715, Intervenor for Repsondent FL Power & Light in 97-1715, Intervenor Rochester Gas & Elec in 97-1715; Intervenor FL Power Corp in 97-1715 [430200-1]. Copies: 6. Certificate of service date 4/16/99. (mcm) [97-1715]

5/18/99 REPLY BRIEF [DISCRIMINATORY DISCOUNTING AND FUNCTIONAL UNBUNDLING] filed by Petitioner Transm Access Plcy in 97-1715, Petitioner Transm Dpndnt Util in 98-1145, Petitioner Enron Power Mkt Inc in 98-1178 [436794-1]. Copies: 7. Certificate of service date 5/18/99. [97-1715, 98-1145, 98-1178] (mcm) [97-1715 98-1145 98-1178]

5/19/99 REPLY BRIEF [STATE COMMISSIONS] filed by Intervenor for Petitioner WA Util Trans Cmsn in 97-1715, Intervenor St NJ Bd Pub Util in 97-1715, Intervenor WY Pub Svc Cmsn in 97-1715, Intervenor for Petitioner Pub Stf NC Util Cmsn in 97-1715, Intervenor for Petitioner NC Util Cmsn in 97-1715,

Intervenor for Petitioner Natl Assn Reg Util in 97-1715, Intervenor FL Pub Svc in 97-1715,k Petitioner People St NY in 98-1111, Petitioner Pub Svc Cmsn St NY in 98-1111, Petitioner VA St Corp Cmsn in 98-1142, Petitioner VT Dept Pub Srvc in 98-1148, Petitioner OH Consum Coun in 98-1150, Petitioner Natl Assn St Util in 98-1155 [436812-1]. Copies: 7. Certificate of service date 5/18/99. [97-1715, 98-1111, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155] (mcm) [97-1715 98-1111 98-1142 98-1147 98-1148 98-1150 98-1155]

8/19/99 FINAL BRIEF filed by Intervenors for Respondent, Enron Power Marketing, Inc., Electricity Consumers Resource Council, American Public Power Association, NE TX Elec Coop Inc, Sam Rayburn Elec G&T, Tex-La Elec Coop TX, Natl Rural Electric Cooperative Assoc., et al. in 97-1715 [458098-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS JOINT BRIEF FOR ALL OTHER INTERVENORS IN SUPPORT OF RESPONDENT]. (lvs) [97-1715]

8/19/99 FINAL BRIEF filed by Petitioners Transm Access Plcy, Transm Dpndnt Util, Enron Power Mkt Inc [488131-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS INITIAL BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP, ENRON POWER MARKETING, INC. AND TRANSMISSION DEPENDENT UTILITY SYSTEMS ON FUNCTIONAL UNBUNDLING AND DISCOUNTING]. [97-

1715, 98-1145, 98-1178] (lvs) [97-1715 98-1145 98-1178]

8/19/99 FINAL REPLY BRIEF filed by Petitioners Transm Access Plcy, Transm Dpndnt Util, Enron Power Mkt Inc [458144-1]. Copies: 15. Certificate of service date 8/19/99. [STYLED AS REPLY BRIEF OF THE TRANSMISSION ACCESS POLICY STUDY GROUP, ENRON POWER MARKETING, INC. AND TRANSMISSION DEPENDENT UTILITY SYSTEMS ON FUNCTIONAL UNBUNDLING AND DISCOUNTING]. [97-1715, 98-1145, 98-1178] (lvs) [97-1715 98-1145 98-1178]

8/20/99 FINAL BRIEF for the Public Service Commissions of New York, Arkansas and Florida, ID Pub Util Cmsn, NC Util Cmsn, WY Pub Svc Cmsn, NJ Board of Public, VA Corp Cmsn, WA Util Trans Cmsn, VT Dept Pub Srvc, Natl Assn Reg Util [458523-1]. Copies: 15. Certificate of service date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1162 98-1169]

8/20/99 FINAL REPLY BRIEF filed by Petitioners/Intervenors VA St Public Service Commissions of NY, AR and FL, Natl Assn of Regulatory Util Cmsn, Pub Util Cmsn ID, NC and WY, NJ Board Pub Util, VA Corp Cmsn, WA Util Trans Cmsn, VT Dept Pub Srvc, OH Consum Coun, Natl Assn St Util [458643-1]. Copies: 15. Certificate of service

date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1150 98-1155 98-1162 98-1169]

8/20/99 APPENDIX [VOLUME I & II] OF LEGISLATIVE HISTORY FOR STATE COMMISSIONS' BRIEF filed by Petitioners/Intervenors Pub Svc Cmsn NY, AR, FL, Natl Assn of Regulatory Util Cmsn, Pub Util Cmsn ID, NC and WY, NJ Board Pub Util, VA Corp Cmsn, WA Util/Trans Cmsn, VT Dept Pub Srvc, OH Consum Coun [458663-1]. Copies: 10. Certificate of service date 8/19/99. [97-1715, 98-1142, 98-1147, 98-1148, 98-1150, 98-1155, 98-1162, 98-1169] (lvs) [97-1715 98-1142 98-1147 98-1148 98-1150 98-1155 98-1162 98-1169]

RELEVANT DOCKET ENTRIES BEFORE FEDERAL ENERGY REGULATORY COMMISSION

Issuance 19980421-0175	3/4/97	Ltr to Vice President A Gore, Jr providing final rules issued on promoting wholesale competition through open access non-discriminatory transmission servs by public utils etc under RM95-8 et al. Portland General Elec Co submits.
Submittal 19960530-0195	5/24/96	Motion for rehearing of Public Serv Commission of New York of Order 888 & 889 re open access transmission & stranded costs under RM95-8 & RM94-7.
Submittal 19960530-0202	5/24/96	Pennsylvania Public Util Commission member J Hanger submits ltr of dissent re 960523 petition for rehearing of Order 888 under RM95-8 & RM94-7.
Submittal	5/24/96	Appl of Coalition for

19960530-0279		Competitive Elec Market for reconsideration & clarification or in alternative rehearing of FERC's Order 888 re promoting wholesale competition etc.
Submittal 19960530-0188	5/23/96-5/24/96	Request of Virginia State Corp Commission for rehearing of Order 888 re open access transmission etc under RM94-7 & RM95-8.
Issuance 19960425-0263	4/24/96	Order 888 final rule re promoting wholesale competition thru open access nondiscriminatory svc/recovery of stranded costs by public utils. Corrected Hoecker.
Submittal 19950811-0061	8/7/95-8/10/95	Comments of NC Utilities Commission re notice of proposed rulemaking & suppl notice of proposed rulemaking re recovery of stranded cost by public utilities etc under RM95-8, et al.

NOTICE OF PROPOSED RULEMAKING - RECOVERY OF STRANDED COSTS BY PUBLIC UTILITIES AND TRANSMITTING UTILITIES IN DOCKET NO. RM-94-7-000
59 FED. REG. 35,274; 35,283-86

[pp. 35,274; 35,283-86]

[35,274]

SUMMARY: The Commission is proposing to amend its regulations to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and transmitting utilities under sections 205, 206, 211 and 212 of the Federal Power Act. The Commission seeks public comment concerning the issues raised by the proposed rulemaking.

DATES: Written comments must be received by the Commission by September 9, 1994. Reply comments must be received by the Commission by October 11, 1994.

ADDRESSES: Send comments to: Office of the Secretary, Federal Energy Regulatory Commission, 825 North Capitol Street, NE., Washington, DC 20426.

FOR FURTHER INFORMATION CONTACT:

James H. Douglass, Office of the General Counsel, Federal Energy Regulatory Commission, 825 North Capitol Street, NE., Washington, DC 20426; Telephone: (202) 208-2143 (legal issues).

Michael A. Coleman, Office of Electric Power Regulation, Federal Energy Regulatory Commission, 825 North Capitol

Street, NE., Washington, DC 20426; Telephone: (202) 208-1236 (technical issues).

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the **Federal Register**, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in room 3104, at 941 North Capitol Street, NE., Washington, DC 20426.

The Commission Issuance Posting System (CIPS), an electronic bulletin board service, provides access to the texts of formal documents issued by the Commission. CIPS is available at no charge to the user and may be accessed using a personal computer with a modem by dialing (202) 208-1397. To access CIPS, set your communications software to use 300, 1200, or 2400 bps, full duplex, no parity, 8 data bits and 1 stop bit. CIPS can also be accessed at 9600 bps by dialing (202) 208-1781. The full text of this order will be available on CIPS for 30 days from the date of issuance. The complete text on diskette in WordPerfect format may also be purchased from the Commission's copy contractor, La Dorn Systems Corporation, also located in room 3104, 941 North Capitol Street, NE., Washington, DC 20426.

Notice of Proposed Rulemaking

June 29, 1994.

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I. Introduction

The Federal Energy Regulatory Commission (Commission) seeks public comment on amending its regulations to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and

transmitting utilities under sections 205, 206, 211 and 212 of the Federal Power Act (FPA).[1] Wholesale stranded costs are defined as any legitimate, prudent and verifiable costs incurred by a public utility or a transmitting utility to provide service to a wholesale requirements customer that subsequently becomes, in whole or in part, an unbundled transmission services customer[2] of that public utility or transmitting utility. Retail stranded . . .

[35283]

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[1]A public utility is defined under section 201(e) of the FPA as "any person who owns or operates facilities subject to the jurisdiction of the Commission under this Part (other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212)." A transmitting utility is defined under section 3(23) of the FPA as "any electric utility, qualifying cogeneration facility, qualifying small power production facility, or Federal power marketing agency which owns or operates electric power transmission facilities which are used for the sale of electric energy at wholesale." Not all transmitting utilities are public utilities. For instance, a municipally-owned electric utility that owns transmission facilities which are used for the sale of electric energy at wholesale is a transmitting utility, but is not a public utility.

[2]An unbundled transmission services customer is one who purchases transmission as a product that is separate from the purchase of generation.

6. Recovery of Retail Stranded Costs

As discussed earlier, there are two general ways in which retail stranded costs are likely to occur:[50] (1) A retail franchise customer may, through State or local government action, become a wholesale customer who can then obtain unbundled transmission services in order to reach a new power supplier;[51] (2) a retail franchise customer may obtain voluntary unbundled retail transmission services from its existing power supplier in order to reach a new power supplier, or there may be a State or local action that results in the existing supplier **[35,281]** providing such retail transmission services.

In the first example (a retail franchise customer becomes an unbundled wholesale power and transmission customer), the Commission clearly has exclusive jurisdiction under sections 201, 205 and 206, or section 212 of the FPA, over the rate for the wholesale interstate transmission services[52] used by the new wholesale entity in order to reach its new generation supplier. In the second example, in which

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[50]Retail stranded costs may result from "self-help" actions such as customer self-generation, and this has long been a fact of life for utilities. *See, supra*, n.18. This proceeding does not address these situations.

[51]In addition, certain retail customers may become retail customers of a newly-created wholesale entity.

[52]Under FPA section 211, the Commission's authority to order wheeling does not turn on whether the transmission services will be in interstate commerce.

a retail franchise customer becomes a retail unbundled transmission customer of its former franchise utility, and a retail power customer of another utility, we conclude that we also have exclusive jurisdiction over the rates, terms and conditions for the retail interstate transmission services.[53]

(i) Jurisdictional Analysis

The Commission's jurisdiction over the rates, terms and conditions of transmission in interstate commerce derives from Congress' power to regulate interstate commerce under the United States Constitution[54] and the FPA. When Congress enacted the FPA, it gave the Commission exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. The Supremacy Clause of the Constitution provides that federal laws enacted pursuant to the powers delegated to the federal government by the United States Constitution are the supreme law of the land.[55] Accordingly, to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service

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[53]We make no determination here regarding the physical or jurisdictional distinctions between transmission and local distribution. Section 201(b)(1) of the FPA states that the Commission has no jurisdiction, except as specifically provided in Parts II and III of the FPA, over facilities used for local distribution. Nor do we address here whether States have authority to order retail wheeling in interstate commerce.

[54]U.S. Const. Art. I, § 8, cl.3.

[55]U.S. Const. Art. VI, cl.2.

are subject to the exclusive jurisdiction of the Commission, and the rates for such service must be filed with the Commission.[56]

Section 201 of the FPA, by its very words, does not limit the Commission's jurisdiction over transmission to transmission of electric energy in interstate commerce sold at wholesale.

Subsection 201(b)(1) of the FPA provides:

(b)(1) The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * * The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy * * *

16 U.S.C. § 824(b)(1).

Much of the legislative history of the FPA indicates that Congress intended the Commission's jurisdiction to extend only to those matters which the *Attleboro* decision[57] held to be beyond the reach of the States. For instance, the

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[56]*See* Montana-Dakota Utilities Co. v. Northwestern Public Service Co., 341 U.S. 246, 251-52 (1951) (*Montana-Dakota*).

[57]Public Utilities Commission v. Attleboro Steam & Electric Co., 273 U.S. 83 (1927) (*Attleboro*). In *Attleboro*, the Supreme Court held that State regulation of the interstate sale of electricity was barred by the Commerce Clause because such regulation would impose a "direct burden" on interstate commerce.

report accompanying the Senate bill states that subsection (b) "leaves to the States the authority to fix local rates even in cases where the energy is brought in from another state."[58] The Senate report also states:

> The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in [*Attleboro*] to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines. * * *

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). Thus, federal jurisdiction over transmission lines is not dependent on whether those lines are used to effect a sale, wholesale or otherwise.

While the provisions of section 201 reserving certain regulatory authority to the States have been interpreted narrowly,[59] the courts have construed "in interstate commerce" broadly. The term does not turn on whether the

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[58]S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). *See also* H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

[59]While Congress may exercise its Commerce Clause authority to grant the States that "ability to restrict the flow of interstate commerce that they would not otherwise enjoy," Lewis v. BT Investment Managers, Inc., 447 U.S. 27, 44 (1980), States may not exercise such regulatory powers unless Congress has expressly stated its intention to make such an affirmative grant of power. New England Power Co. v. New Hampshire, 55 U.S. 331, 343 (1982).

contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce.

For example, in *Jersey Central Power & Light Co. v. FPC*, 319 U.S. 61 (1943), the Court stated:

> It is impossible for us to conclude that this definition [of transmission in interstate commerce] means less than it says and applies only to the energy at the instant it crosses the state line and so only to the facilities which cross the line and only to the company which owns the facilities that cross the line.

319 U.S. at 71. Thus, a critical question regarding the jurisdictional status of a wheeling transaction is whether the facilities used to provide the service transmit electric energy in interstate commerce. *See also Connecticut Light & Power Co. v. FPC*, 324 U.S. 515 (1945) (CL&P); *FPC v. Florida Power & Light Co.*, 404 U.S. 453 (1972). In *CL&P*, the Court emphasized that whether certain facilities transmit electric energy in interstate commerce is more a technical than a legal question. The Court stated, "[f]ederal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test." 324 U.S. at 529.

In all of the above cases, the Court's decisions turned on whether energy flowed in interstate commerce as a technical matter. The decisions did not turn on whether the energy flowing in interstate commerce was being sold for

resale or was being sold to an end user. However, under FPA section 201(b), the Commission does not have jurisdiction over facilities used in local distribution. In *CL&P*, the Court stated that local distribution facilities are exempt from Commission jurisdiction even if those facilities "carry no energy except extra-state energy." 324 U.S. at 531. The Court rejected the argument that transmission and local distribution facilities could be distinguished by the proportion or amount of interstate energy that they carried:

> We do not find that Congress has conditioned the jurisdiction of the Commission upon any particular volume or proportion of interstate energy involved, and we do not think it would be appropriate to supply such a jurisdictional limitation by construction.

324 U.S. at 536. The determination of whether facilities are local distribution facilities remains a factual matter to be decided in the first instance by the Commission. *See FPC v. Southern California Edison Co.*, 376 U.S. 205 (1964).

While the precise demarcation between transmission and local distribution remains unclear, and the Commission has not yet definitively addressed this issue, there is nothing in the statute, its legislative history, or the case law to indicate that the Commission's jurisdiction over rates, terms and conditions of transmission in interstate commerce extends only to **[35,285]** wholesale transmission and not retail transmission.

(ii) Treatment of Retail Costs

Because the Commission has jurisdiction over the rates, terms and conditions of both wholesale and retail transmission services in interstate commerce by public utilities, arguably it may allow retail stranded cost recovery in rates for either wholesale or retail transmission services. There nevertheless may be important legal or policy reasons to exclude retail stranded costs from transmission rates. As noted earlier, however, the Commission has been presented only with the question of whether it should permit public utilities to seek recovery in *wholesale* transmission rates of stranded investment costs incurred to serve former retail customers (Scenario 2, section III.A.). The Commission has not been presented with the question of whether it should permit public utilities to seek recovery in *retail* transmission rates of stranded costs incurred to serve the customer when it was a retail customer (Scenario 3, section III.A.).

While we believe the Commission has the authority to address retail stranded costs through its jurisdiction over the rates, terms and conditions of interstate transmission services used by retail or newly-created wholesale customers, we also believe that the recovery of the costs of transition to competition at the retail level is a matter that should be addressed by State authorities. This is because retail stranded costs will occur primarily as a result of State and local decisionmaking regarding retail franchise areas and the creation of new wholesale entities. In particular, the Commission believes it is incumbent upon states to deal with the consequences of stranded costs that occur as a result of retail wheeling. Our strong policy preference is that states explicitly address the issue. State and local decisionmakers

have a first-hand understanding of the regulatory bargain with respect to stranded costs incurred to serve retail customers, and they are familiar with the planning, investment and purchase activities of the utilities they regulate.

There are a number of procedural mechanisms which we believe States can use to address retail stranded costs. For example, a State that permits a retail franchise customer to become a wholesale entity may consider whether to impose an exit fee prior to, or as a condition of, creating the wholesale entity. Similarly, a State may consider whether to require payment of an exit fee prior to a franchise customer being permitted to obtain unbundled retail wheeling. In situations in which local distribution facilities are used by a retail wheeling customer, the State may consider whether to allow recovery of stranded costs through rates for local distribution services. If a State decides not to impose exit fees, or a surcharge through distribution rates, it may consider whether to allow recovery of stranded costs from remaining customers.

In situations in which a new wholesale entity obtains ownership or control of a franchise utility's transmission or distribution facilities, it is possible that State condemnation proceedings will provide a forum for a utility to seek recovery of any stranded costs. *What types of payments, if any, do new municipal utilities make to prior service providers? Do these reimbursements allow for recovery of stranded generation costs? Is there variation among the States as to the legal ability of local entities to municipalize? Is there variation among the States as to the payments made by new municipal utilities to previous suppliers?*

There may, of course, be other mechanisms which States can use to determine whether to allow stranded cost recovery, and from whom to allow recovery. *The Commission solicits comments on what other mechanisms might be used, and whether these mechanisms are adequate to deal with retail stranded costs.*

While our strong preference is for States to address retail stranded costs in whatever way they deem appropriate, we are willing to explore whether there are circumstances under which this Commission should consider claims for recovery of retail stranded costs. *We will therefore present two proposed alternatives regarding retail stranded costs, and seek comment on both.* However, as noted above, we express no preference in favor of either alternative.

Under the first alternative, the proposed rule provides that if in a specific circumstance an appropriate State authority explicitly considers and deals with retail stranded costs and there is no conflict within or among State regulatory bodies regarding a State's disposition of the issue, this Commission will not entertain a request for retail stranded cost recovery. However, in the absence of a clear expression by an appropriate State authority that it has dealt with the issue, or in the event of a conflict between States[60] or among State

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[60]For example, a conflict between States could result if State A's legislature allows a former retail customer to become a wholesale entity and the wholesale entity obtains transmission services so that it now takes only one half of its 100 MW load from its current utility supplier, which is a multistate utility. As a result of State A's action, the utility has retail stranded costs for 50 MW of generation. State A's commission allocates the utility's retail

officials within a single state, the Commission proposes to entertain requests to recover retail stranded costs.

Under the second alternative, the proposed rule provides that the Commission will not entertain any request for recovery of retail stranded costs. Under this proposal, State or local authorities will be the only forum for addressing the issue. The aforementioned preference for States to address retail stranded costs in whatever way they deem appropriate, the need for regulatory certainty, and the States' knowledge and expertise regarding utility planning, investment and purchase activities arguably favors the second alterative. *However, we solicit comment on whether there should be limited exceptions to the second alternative rule.*

As to both alternatives, the Commission solicits comments on the following questions.

Are there circumstances under which it is not necessarily appropriate to defer to the States (e.g., where one State takes an action regarding retail stranded costs which has adverse consequences for another State)? Are there circumstances under which a State may not have an adequate mechanism for addressing retail stranded costs, and may want the Commission to provide a forum?

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costs so that State A's retail customers are responsible for only one half of the stranded costs. State B's commission, the other State in which the utility operates, allocates the utility's retail costs so that none of the retail stranded costs are allocated to State B's retail customers.

If a State does not explicitly address stranded costs resulting from an action that allows retail customers to purchase from a supplier other than the franchised utility, should this Commission entertain requests from the utilities left with the stranded costs? Beyond silence from the State, are there other factors that the Commission should consider before accepting requests for retail stranded cost recovery? Specifically, would financial health and possible adverse impacts on reliability be sufficient reason for Federal action?

The Commission further solicits comments on the following questions:

(1) Does the Commission have legal authority to allow retail stranded costs in rates for wholesale transmission services? Should the Commission do so as a matter of policy? If so, which costs?

(2) Does the Commission have legal authority to allow retail stranded costs **[35,286]** *in rates for retail transmission service? Should the Commission do so as a matter of policy? If so, which costs?*

(3) Does FPA section 212 give the Commission legal authority to allow recovery of retail stranded costs in rates for wholesale transmission services under FPA section 211?

(4) Are there legal or policy reasons why in Scenario 2 (p. 15), the Commission should entertain requests for recovery of retail stranded costs in wholesale transmission rates, but should not entertain requests for recovery of retail stranded costs in retail transmission rates in Scenario 3 (section III.A.)?

If the Commission determines that it will entertain requests for recovery of retail stranded costs through rates for wholesale or retail transmission in interstate commerce, the Commission proposes not to apply the "reasonable expectation" test used for wholesale stranded costs. To apply such a test would require a hearing on whether the franchise utility had a reasonable expectation, *e.g.*, of having its franchise renewed, of municipalization occurring, or of a section 212(h) non-sham wholesale entity being created by the State or local authority. No such test appears warranted because, in general, there is at the retail level an obligation to serve which is much stronger than any contractual obligation to serve at the wholesale level. The regulatory compact that has governed provision of retail service includes an implicit obligation to purchase concomitant with the utility's obligation to serve.

The Commission requests comments on whether these assumptions are correct, i.e., is the reasonable expectation test inapplicable to retail stranded costs? Are there situations, for instance, in which utilities could have expected municipalization to occur based on an established course of dealing?

Based on these assumptions, if the Commission determines that it will entertain requests for retail stranded costs, the proposed regulations for retail stranded costs would require only a showing of the dollar amounts that have been stranded as a result of the retail customer no longer taking bundled service from the franchise utility's system. In essence, this results in direct assignment of retail stranded costs to the former franchise customer. *The Commission requests comments on how to determine retail stranded costs*

as a general matter. Is there a future time when a retail customer's action of leaving a local franchise no longer has any adverse economic consequences on the franchise utility? If so, what is an appropriate way to make such a determination?

[pp. 1-4]

Comments of North Carolina Utilities Commission and the Public Staff of the North Carolina Utilities Commission

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[2]

COMMENTS OF THE
NORTH CAROLINA UTILITIES COMMISSION
AND THE
PUBLIC STAFF - NORTH CAROLINA UTILITIES COMMISSION

TO THE

FEDERAL ENERGY REGULATORY COMMISSION

REGARDING

NOTICE OF PROPOSED RULEMAKING AND
SUPPLEMENTAL
NOTICE OF PROPOSED RULEMAKING

DOCKET NO. RM95-8-000
PROMOTING WHOLESALE COMPETITION
THROUGH OPEN ACCESS NON-DISCRIMINATORY
TRANSMISSION SERVICES BY PUBLIC UTILITIES

DOCKET NO. RM94-7-00 l
RECOVERY OF STRANDED COSTS BY
PUBLIC UTILITIES AND TRANSMITTING UTILITIES

[3]

UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION

[Filed August 10, 1995]

Docket Nos. RM95-8-000 and RM94-7-001

Promoting Wholesale Competition	)
Through Open Access	)
Non-discriminatory Transmission	)
Services by Public Utilities	)
	)
Recovery of Stranded Costs by	)
Public Utilities and Transmitting	)
Utilities	)
	)

INITIAL COMMENTS OF THE NORTH CAROLINA UTILITIES COMMISSION AND THE PUBLIC STAFF-NORTH CAROLINA UTILITIES COMMISSION

The North Carolina Utilities Commission (NCUC) and the Public Staff of the North carolina Utilities Commission (Public Staff) respectfully offer the following comments for consideration by the Federal Energy Regulatory Commission (FERC) in its proposed rulemaking in Docket Nos. RM95-8-000 and RM94-7-001 regarding open access to the electric transmission system and the recovery of stranded costs occasioned by open *access*.

1. OPEN ACCESS SHOULD BE APPROACHED ON A CASE-BY-CASE BASIS.

The NCUC and the Public Staff are concerned that the FERC is proposing a generic remedy for a less-than-generic problem. The FERC position that the anti-discrimination provisions of the Federal Power Act (FPA) require across-the-board tariffs for open access to the electric transmission system of every utility is misguided. We recognize that the FERC and various states may disagree about whether a generic approach to open access is legal.[1] Nevertheless, even assuming that such an approach is legal, we believe that a case-by-case approach to open access would be far preferable from a policy standpoint for a number of reasons.

Discriminatory wholesale wheeling rates and discriminatory denial of wholesale access to the electric, utilities' transmission systems vary greatly among the states and are simply not consistently present to the extent necessary to justify a generic approach to open access. The NCUC is unaware of complaints to the FERC by any wholesale customer regarding discriminatory denial of access to **[3]** or of discriminatory rates for use of the transmission system in North Carolina. The absence of such complaints strongly

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[1]This legal argument, as we understand it, is based on the fact that § 211 of the FPA, 16 U.S.C. § 824j, as amended by § 721 of the Energy Policy Act of 1992 (the source of the FERC's authority to order wholesale wheeling) provides that the FERC can order a transmitting utility to provide transmission service upon application and after notice and an opportunity for an evidentiary hearing. We will be monitoring with great interest the comments of others with respect to this issue.

suggests that discrimination is not a problem in North Carolina.

If anything, the generic open access proposal by the FERC has the potential to cause undue discrimination where none existed before. For example, the electric transmission system of each utility is interconnected with neighboring transmission systems in order to ensure greater reliability. However, this interconnection exposes each transmission system to greater loop flows.[2] Open access will greatly complicate loop flows by increasing the number of participants contributing to such loop flows, and it will also cause an unfairly disproportionate burden of dealing with the impact of loop flows to fall on many utilities that are not direct participants in an open access wheeling transaction.

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[2]As the FERC is well aware, the actual path taken by electric power flow across a transmission system is difficult to predict. Because of its interconnection with neighboring systems, a transmission system typically consists of a number of possible paths between any two points.. Electric current essentially flows on a path of least resistance. An electric load placed on the transmission system will usually cause electric current to flow in all possible paths, but the amount of flow in each path will vary depending on the amount of resistance to flow in a given path. The resulting circuitous route (or mutes) that electric current actually takes in order for electric power to be transferred between two points is called loop flow. In sum, the actual flow of electricity typically diverges significantly from the contract path, with the result that the supposed economics of the contract path frequently have little to do with the actual cost of the power transfer.

Section 211 of the Federal Power Act, as mended by the Energy Policy Act of 1992 (EPACT), provides that an electric utility, power marketing agency or non-utility generator may apply to the FERC for an order requiring access to the electric transmission system ora transmitting utility (including enlargement of transmitting capacity as necessary). Thus, the EPACT clearly contemplates the ordering of wholesale wheeling **upon request**. We believe this reflects a congressional intent for wholesale wheeling to be required on a case-by-case basis and that the FERC should review issues of "undue discrimination" on a case-by-case basis as intended by the EPACT.

The FERC's current generic approach to pricing may well inhibit greater competition in the wholesale generation market. The FERC's authority to require new transmission facilities to be built, for example, is dependent upon the states granting authority for the new facilities to be constructed. Because the granting of a certificate by a state commission for the construction of transmission facilities could well preclude that commission from disallowing recovery in retail rates, many states may be reluctant to grant such authority with little or no assurance that retail ratepayers will not be required by default to carry a disproportionate share of the costs. Of substantial concern in this regard is the fact that many utilities appear to be unwilling to challenge the FERC's authority and/or its determinations with regard to open access because such action is perceived as endangering approval of market based rates for affiliated generating companies. Obviously, to the extent transmission costs are not recovered by the users of the transmission system, there is a danger that the utilities' captive retail ratepayers will end up covering these costs.

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[pp. 6-7]

[6]

3. EACH UTILITY'S GENERATING CAPACITY EXPANSION PLAN REFLECTS AN OBLIGATION TO SERVE THAT TRANSCENDS ITS CONTRACTUAL OBLIGATIONS TO CUSTOMERS.

The NCUC and the Public Staffare concerned about the negative impact that open access to the electric transmission system will have on each utility unless its obligation to serve its wholesale customers is waived. State regulators have charged each utility with an obligation to serve at the retail level in their respective states, and the FERC has created a "de facto" obligation to serve at the wholesale level.

The obligation to serve is reflected in each utility's generating capacity expansion plan, and it transcends any contractual obligation the utility may incur with a customer at either the retail level or the wholesale level. Any "reasonable expectation" that a wholesale customer will remain on a utility's system for the duration of the cost to serve that customer is based on the utility's "de facto" obligation to serve and the resulting generating capacity expansion plan. Until the obligation to serve wholesale customers is clarified, the NCUC and other state commissions will have little choice but to require each utility's integrated resource planning to include the assumption that the obligation to serve extends past the expiration date of its wholesale contracts.

Mandatory wholesale wheeling and a utility's obligation to serve wholesale customers are inconsistent with each other. The obligation to serve arises from a utility's monopoly status. If open access to the electric transmission system is required for wholesale customers in order to promote greater competition, then a utility's obligation to serve them must be waived. Otherwise, the utilities are under a handicap and true competition cannot exist. We urge the FERC to recognize this inconsistency.

4. THE DIVISION OF JURISDICTION BETWEEN THE FERC AND THE STATES IN THE OPEN ACCESS PROPOSED RULEMAKING IS NOT SUPPORTED BY THE FPA OR BY CASE LAW.

The NCUC and the Public Staff are concerned that the division of jurisdiction between the FERC itself and the states in the open access proposed rulemaking is not supported by the FPA or the relevant case law. The FERC open access proposal contains the assertion that the FERC has jurisdiction over all transmission facilities, on the assumption that all transmission facilities are interconnected with neighboring transmission systems and are, therefore, directly or indirectly used [7] to serve wholesale customers. While it is generally recognized that the FERC has jurisdiction over transmission facilities serving wholesale customers and over transmission facilities used for inter-utility transactions, the FISA and the case law provide that the FERC has no jurisdiction over facilities used in local distribution. Local distribution facilities have been defined as facilities used to deliver electric energy to the ultimate consumer. Therefore, because retail customers in many instances are served directly off the transmission

system, transmission facilities can be facilities used in local distribution.

Open access to the transmission facilities that directly serve retail customers will invite sham transactions and sham municipalization by those transmission level retail customers seeking to become wholesale customers and thereby gain access to wholesale wheeling. This is an issue that is certain to invite litigation and potentially delay true wholesale open access. An example of this is the case involving Falls Church, Virginia, and Virginia Electric & Power Company. The NCUC and the Public Staff believe that the FERC has underestimated the creativity with which those individuals who are consultants to large retail customers will approach this issue. A significant cottage industry may well arise solely to convert retail customers into wholesale customers, thereby subverting the intent of Congress as expressly set forth in EPACT.

FEDERAL ENERGY REGULATORY COMMISSION
ORDER 888

[Issued April 24, 1996]

Docket Nos. RM95-8-000 and RM94-7-001

Order No. 888

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[pp. 31,632 - 31,684]

[31,036]
61 F.R. 21540 (May 10, 1996)

18 CFR Parts 35 and 385

Promoting Wholesale Competition Through Open Access Non-Discriminatory Transmission Services by Public Utilities; Recovery of Stranded Costs by Public Utilities and Transmitting Utilities

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Final Rule.

SUMMARY: The Federal Energy Regulatory Commission (Commission) is issuing a Final Rule requiring all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce to have on file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service. The Final Rule also permits public utilities and transmitting utilities to seek recovery of legitimate, prudent

and verifiable stranded costs associated with providing open access and Federal Power Act section 211 transmission services. The Commission's goal is to remove impediments to competition in the wholesale bulk power marketplace and to bring **[31,633]** more efficient, lower cost power to the Nation's electricity consumers.

EFFECTIVE DATE: This Final Rule will become effective on July 9, 1996.

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I. Introduction/Summary

Today the Commission issues three final, interrelated rules designed to remove impediments to competition in the wholesale bulk power marketplace and to bring more efficient, lower cost power to the Nation's electricity consumers.[1] The legal and policy cornerstone of these rules is to remedy undue discrimination in access to the monopoly owned transmission wires that control whether and to whom electricity can be transported in interstate commerce. A second critical aspect of the **[31,635]** rules is to address recovery of the transition costs of moving from a monopoly-regulated regime to one in which all sellers can compete on a fair basis and in which electricity is more competitively priced.

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[1]These rules are the rules on open access and stranded costs in the above dockets (*FERC Statutes and Regulations* ¶31,036), and an accompanying rule on Open Access Same-Time Information System and Standards of Conduct (OASIS Final Rule) (*FERC Statutes and Regulations* ¶31,037) being issued contemporaneously. The Commission also is issuing contemporaneously a notice of proposed rulemaking on capacity reservation open access transmission tariffs in Docket No. RM96-11-000, *FERC Statutes and Regulations* ¶32,517. These final rules and proposed rule are being published concurrently in the *Federal Register*.

In the year since the proposed rules were issued,[2] the pace of competitive changes in the electric utility industry has accelerated. By March of last year, 38 public utilities had filed wholesale open access transmission tariffs with the Commission. Today, prodded by such competitive changes and encouraged by our proposed rules, 106 of the approximately 166 public utilities that own, control, or operate[3] transmission facilities used in interstate commerce have filed some form of wholesale open access tariff. In addition, since the time the proposed rules were issued, numerous state regulatory commissions have adopted or are

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[2]On March 29, 1995, the Commission issued two notices of proposed rulemaking concerning open access transmission and stranded cost recovery. Promoting Wholesale Competition Through Open-Access Non-Discriminatory Transmission Service by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking and Supplemental Notice of Proposed Rulemaking, 60 FR 17662 (April 7, 1995), *FERC Statutes and Regulations* ¶32,514 (1995). On December 13, 1995, the Commission issued a notice of proposed rulemaking on information systems. Real- Time Information Networks and Standards of Conduct, Notice of Proposed Rulemaking, 60 FR 66182 (December 21, 1995), *FERC Statutes and Regulations* ¶32,516 (1995).

[3]The Commission's notice of proposed rulemaking in the above dockets proposed to apply the proposed requirements to public utilities that own and/or control facilities used for the transmission of electric energy in interstate commerce. "Own and/or control" is intended to include public utilities that "operate" facilities used for the transmission of electric energy in interstate commerce. However, we have modified the Final Rule regulatory text to remove any ambiguity.

actively evaluating retail customer choice programs or other utility restructuring alternatives. These events have been spurred by continuing pressures in the marketplace for changes in the way electricity is bought, sold, and transported. Increasingly, customers are demanding the benefits of competition in the growing electricity commodity market.

The Commission estimates the potential quantitative benefits from the Final Rule will be approximately $3.8 to $5.4 billion per year of cost savings, in addition to the non-quantifiable benefits that include better use of existing assets and institutions, new market mechanisms, technical innovation, and less rate distortion. The continuing competitive changes in the industry and the prospect of these benefits to customers make it imperative that this Commission take the necessary steps within its jurisdiction to ensure that all wholesale buyers and sellers of electric energy can obtain non-discriminatory transmission access, that the transition to competition is orderly and fair, and that the integrity and reliability of our electricity infrastructure is maintained.

In this Rule, the Commission seeks to remedy both existing and future undue discrimination in the industry and realize the significant customer benefits that will come with open access. Indeed, it is our statutory obligation under sections 205 and 206 of the Federal Power Act (FPA) to remedy undue discrimination.

To do so, we must eliminate the remaining patchwork of closed and open jurisdictional transmission systems and ensure that all these systems, including those that already provide some form of open access, cannot use monopoly

power over transmission to unduly discriminate against others. If we do not take this step now, the result will be benefits to some customers at the expense of others. We have learned from our experience in the natural gas area the importance of addressing competitive transition issues early and with as much certainty to market participants as possible.

Accordingly, in this proceeding and in the accompanying proceeding on OASIS, the Commission, pursuant to its authorities under sections 205 and 206 of the FPA:

•Requires all public utilities that own, control or operate facilities used for transmitting electric energy in interstate commerce

•To file open access non-discriminatory transmission tariffs that contain minimum terms and conditions of non-discriminatory service;

[31,636]

•To take transmission service (including ancillary services) for their own new wholesale sales and purchases of electric energy under the open access tariffs;

•To develop and maintain a same-time information system that will give existing and potential transmission users the same access to transmission information that the public utility enjoys, and further requires public utilities to separate transmission from generation marketing functions and communications;

•Clarifies Federal/state jurisdiction over transmission in interstate commerce and local distribution and provides for deference to certain state recommendations; and

•Permits public utilities and transmitting utilities to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and FPA section 211 transmission services.

Open Access

The Final Rule requires public utilities to file a single open access tariff that offers both network, load-based service and point-to-point, contract-based service. The Rule contains a pro forma tariff that reflects modifications to the NOPR's proposed terms and conditions and also permits variations for regional practices. All public utilities subject to the Rule, including those that already have tariffs on file, will be required to make section 206 compliance filings to meet the new pro forma tariff non-price minimum terms and conditions of non-discriminatory transmission. Utilities may propose their own rates in a section 205 compliance filing.

The Rule provides that public utilities may seek a waiver of some or all of the requirements of the Final Rule. In addition, non-public utilities may seek a waiver of the tariff reciprocity provisions.

The Final Rule does not generically abrogate existing requirements contracts, but will permit customers and public utilities to seek modification, or termination, of certain existing requirements contracts on a case-by-case basis. As to coordination arrangements and contracts, the Rule finds that

these arrangements and contracts may need to be modified to remove unduly discriminatory transmission access and/or pricing provisions. Such arrangements and agreements include power pool agreements, public utility holding company agreements, and certain bilateral coordination agreements. The Rule provides guidance and timelines for modifying unduly discriminatory coordination arrangements and contracts, and specifies when the members of such arrangements must begin to conduct trade with each other using the same open access tariff offered to others. The Rule also provides guidance regarding the formation of independent system operators (ISOs).

The Rule does not require any form of corporate restructuring, but will accommodate voluntary restructuring that is consistent with the Rule's open access and comparability policies.

As discussed in the NOPR, not all owners or controllers of interstate transmission facilities are subject to the Commission s jurisdiction under sections 205 and 206 of the FPA and therefore are not subject to this Rule's open access requirements. Therefore, the Final Rule retains the proposed reciprocity provision in the pro forma tariff. Without such a provision, non-open access utilities could take advantage of the competitive opportunities of open access, while at the same time offering inferior access, or no access at all, over their own facilities. Thus, open access utilities would be unfairly burdened. We note that some non-jurisdictional utilities have expressed an interest in a mechanism for obtaining a Commission determination that their transmission tariffs satisfy the reciprocity provisions in

the pro forma tariffs, and we provide such a mechanism in the Rule.

The Final Rule does not generically provide for market-based generation rates. Although the Rule codifies the Commission's prior decision that there is no generation dominance in new generating capacity, intervenors in cases may raise generation dominance issues related to new capacity. In addition, to obtain market-based rates for existing generation, we will continue to require public utilities to show, on a case-by-case basis, that there is no generation dominance in existing capacity. Further, in all market-based rate cases, we will continue to look at whether an applicant and its affiliates could erect other barriers to entry and **[31,637]** whether there may be problems due to affiliate abuse or reciprocal dealing.

Finally, contemporaneously with this Rule the Commission issues a NOPR on capacity reservation tariffs as an alternative, and perhaps superior, means of remedying undue discrimination.

Transmission/Local Distribution

The Rule clarifies the Commission's interpretation of the Federal/state jurisdictional boundaries over transmission and local distribution. While we reaffirm our conclusion that this Commission has exclusive jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, we nevertheless recognize the very legitimate concerns of state regulatory authorities as they contemplate direct retail access or other state restructuring programs. Accordingly, we specify

circumstances under which we will give deference to state recommendations. Although jurisdictional boundaries may shift as a result of restructuring programs in wholesale and retail markets, we do not believe this will change fundamental state regulatory authorities, including authority to regulate the vast majority of generation asset costs, the siting of generation and transmission facilities, and decisions regarding retail service territories. We intend to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies.

Stranded Costs

With regard to stranded costs, the Final Rule adopts the Commission's supplemental proposal. It will permit utilities to seek extra-contractual recovery of stranded costs associated with a limited set of existing (executed on or before July 11, 1994) wholesale requirements contracts and provides that the Commission will be the primary forum for utilities to seek recovery of stranded costs associated with retail-turned-wholesale transmission customers. It also will allow utilities to seek recovery of stranded costs caused by retail wheeling only in circumstances in which the state regulatory authority does not have authority to address retail stranded costs at the time the retail wheeling is required. The Rule retains the revenues lost approach for calculating stranded costs and provides a formula for calculating such costs.

Environmental Issues

The Commission has prepared a Final Environmental Impact Statement (FEIS) evaluating the possible

environmental consequences of changes in the bulk power marketplace expected to occur as a result of the open access requirements of this Final Rule. The FEIS focuses, as do most commenters, on possible increases in emissions of nitrogen oxides (NO/X/) from certain fossil-fuel fired generators, which could affect air quality in the producing region and in areas to which these emissions may be carried.

In response to comments on the Draft EIS, the Commission performed numerous additional studies. The FEIS finds that the relative future competitiveness of coal and natural gas generation is the key variable affecting the impact of the Final Rule. If competitive conditions favor natural gas, the Rule is likely to lead to environmental benefits. Both EPA and the Commission staff believe this projected scenario is the more likely one. If competitive conditions favor coal, the Rule may lead to small negative environmental impacts. However, even using the most extreme, unlikely assumptions about the future of the industry, the negative consequences are not likely to occur until after the turn of the century. Because the impacts will remain modest at least until 2010, there is no need for an interim mitigation program. In addition, even if the data showed more significant negative consequences requiring mitigation, the Commission does not have the statutory authority under the Federal Power Act or the expertise to address this possible far- term problem. The Commission believes, however, that there is time for federal and state air quality authorities to address any potential adverse impact as part of a comprehensive NO_x regulatory program under the Clean Air Act.[4]

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[4]42 U.S.C. §7401, et seq.

Despite our conclusions regarding the lack of environmental impacts expected to result from the Rule, the Commission has examined a wide variety of proposals for mitigating possible adverse effects. We share the view of most commenters **[31,638]** that the preferred approach for mitigating increased NO/X/ emissions generally is a NO/X/ cap and trading regulatory program comparable to that developed by Congress to address sulfur dioxide emissions in the Clean Air Act Amendments of 1990.[5] The Commission has examined various means of establishing such a program, including use of existing federal authorities under the Clean Air Act, cooperative efforts by state and federal air quality regulators, and development of a new emissions regulatory program administered by the Commission under the Federal Power Act. The Commission has concluded that a NO/X/ regulatory program could best be developed and administered under the Clean Air Act, in cooperation with interested states, and offers to lend Commission support to that effort should it become necessary.

Conclusion

The Commission believes that the Final Rule will remedy undue discrimination in transmission services in interstate commerce and provide an orderly and fair transition to competitive bulk power markets.

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[5]42 U.S.C.A. §7651b-e.

II. Public Reporting Burden

The Open Access Final Rule and the Stranded Cost Final Rule specify filing requirements to be followed by public utilities that own, control or operate transmission facilities in interstate commerce in making non-discriminatory open access tariff filings and filings to recover legitimate, prudent and verifiable stranded costs. The information collection requirements of the final rules are attributable to FERC-516 "Electric Rate Filings." The current total annual reporting burden for FERC-516 is 828,300 hours.

A. *Docket No. RM95-8-000 (Open Access Final Rule)*

The Open Access Final Rule requires public utilities filing non-discriminatory open access tariffs to provide certain information to the Commission. The Commission estimated that the public reporting burden for the information collection would average 300 hours per response. This estimate included time for reviewing the requirements of the Commission's regulations, searching existing data sources, gathering and maintaining the necessary data, completing and reviewing the collection of information, and filing the revised information. No comments on the burden estimate were received. Because the Final Rule adopts essentially the same information requirements that are contained in the proposed rule, we believe that the average filing burden is same for the Final Rule.

In the proposed rule, the Commission noted that there are approximately 328 public utilities, including marketers and wholesale generation entities. We initially estimated that 137 public utilities own, control or operate facilities used for

the transmission of electric energy in interstate commerce, and would be subject to the filing requirements of the proposed rule. Upon further review, the Commission believes that approximately 166 public utilities will respond to the information collection. Accordingly, the public reporting burden is estimated to be 49,800 hours.

B. *Docket No. RM94-7-001 (Stranded Cost Final Rule)*

In the supplemental notice of proposed rulemaking, the Commission estimated that the information requirements of the proposed rule would not differ substantially from those contained in the initial proposed rule. In that notice, the Commission estimated that the public reporting burden for the information requirements contained in the proposed rule would be 50 hours per response with 10 responses annually. No comments on this filing burden were received. The information requirements adopted in the Stranded Cost Final Rule are not substantially different from those in the proposed rule. Therefore, the Commission concludes that there will be no additional public filing burden associated with the Stranded Cost Final Rule.

III. Background

In the NOPR, we set out a detailed statement of the events leading up to this rulemaking. We repeat that background here, updated to reflect what has happened since March 1995, and discuss why it is necessary to undertake regulatory reform in the electric industry at this time. We do so to provide the necessary **[31,639]** backdrop to our action in adopting this Rule.

A. *Structure of the Electric Industry at Enactment of Federal Power Act*

The Federal Power Act was enacted in an age of mostly self-sufficient, vertically integrated electric utilities, in which generation, transmission, and distribution facilities were owned by a single entity and sold as part of a bundled service (delivered electric energy) to wholesale and retail customers. Most electric utilities built their own power plants and transmission systems, entered into interconnection and coordination arrangements with neighboring utilities, and entered into long-term contracts to make wholesale requirements sales (bundled sales of generation and transmission) to municipal, cooperative, and other investor-owned utilities (IOUs) connected to each utility's transmission system. Each system covered limited service areas. This structure of separate systems arose naturally due primarily to the cost and technological limitations on the distance over which electricity could be transmitted.

Through much of the 1960s, utilities were able to avoid price increases, but still achieve increased profits, because of substantial increases in scale economies, technological improvements, and only moderate increases in input prices.[6] Thus, there was no pressure on regulatory

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[6]Paul L. Joskow, Inflation and Environmental Concern: Structural Change in the Process of Public Utility Regulation, 17 J. Law & Econ. 291, 312 (1974); *see also* Charles F. Phillips, Jr., *The Regulation of Public Utilities* 11 (1988).

commissions to use regulation to affect the structure of the industry.[7]

B. *Significant Changes in the Electric Industry*

In the late 1960s and throughout the 1970s, a number of significant events occurred in the electric industry that changed the perceptions of utilities and began a shift to a more competitive marketplace for wholesale power.[8] This was the beginning of periods of rapid inflation, higher nominal interest rates, and higher electricity rates.[9] During this time, consumers became concerned about higher electricity rates and questioned any price increases filed by utilities.[10]

During this same time frame, the construction of nuclear and other capital-intensive baseload facilities--actively encouraged by federal and some state governments--contributed to the continuing cost increases and uncertainties

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[7]*See* Joskow, *supra* at p. 312; *see also* Phillips, *supra* at p. 12.

[8]*See* Joskow, *supra* at p. 312; *see also* Phillips, *supra* at pp. 12-13.

[9]*See* Joskow, *supra* at pp. 312-13; *see also* Phillips, supra at p. 13. The Arab oil embargo resulted in significantly higher oil prices through the 1970s. *See* Richard J. Pierce, Jr., The Regulatory Treatment of Mistakes in Retrospect: Canceled Plants and Excess Capacity, 132 U. Pa. L. Rev. 497, 501 (1984).

[10]*See* Joskow, *supra* at p. 313; *see also* Phillips, *supra* at p. 13.

in the industry.[11] These investments were made based on the assumptions that there would be steady increases in the demand for electricity and continued large increases in the price of oil.[12] However, due to conservation and economic downturns, the expected demand increases did not materialize. Load growth virtually disappeared in some areas, and many utilities unexpectedly found themselves with excess capacity.[13] In addition, by the 1980s, the oil cartel collapsed, with a resulting glut of low-priced oil.[14] At the same time, inflation substantially increased the costs of these large baseload generating plants.[15] Surging interest rates further increased the cost of the capital needed to finance and capitalize these projects and completion schedules were

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[11]*See generally Jersey Central Power & Light Company v. FERC*, 810 F.2d 1168, 1171 (D.C. Cir. 1987).

[12]*Id.*

[13]*See* Pierce, *supra* at 503. By 1983, the Department of Energy had estimated that the sunk costs for canceled nuclear plants alone amounted to $10 billion. *Id.* at 498.

[14]*Id.*

[15]*See* Bernard S. Black & Richard J. Pierce, Jr., The Choice Between Markets and Central Planning in Regulating the U.S. Electricity Industry, 93 Col. L. Rev. 1339, 1346 (1993) ("Actual costs of nuclear power plants vastly exceeded estimates, sometimes by as much as 1000%.").

significantly **[31,640]** extended by, in part, more stringent safety and environmental requirements.[16]

As a result, expensive large baseload plants for which there was little or no demand, came onto the market or were in the process of being constructed. Accordingly, between 1970 and 1985, average residential electricity prices more than tripled in nominal terms, and increased by 25% after adjusting for general inflation.[17] Moreover, average electricity prices for industrial customers more than quadrupled in nominal terms over the same period and increased 86% after adjusting for inflation.[18] The rapidly increasing rates for electric power during this period, together with the opportunities provided by the Public Utility Regulatory

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[16]*See* Phillips, *supra* at p. 13. Fossil fuel-fired plants became subject to increased regulation as a result of the Clean Air Act of 1970, and its 1977 amendments. 42 U.S.C. §§7401-7642. In 1971, nuclear plant licensing became subject to the environmental impact statement requirements of the National Environmental Policy Act of 1969. 42 U.S.C. §4332. Following the 1979 accident at the Three Mile Island nuclear plant, nuclear plants also became subject to additional safety regulations, resulting in higher costs. *See* Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 35. Between 1976 and 1980, most states and many localities instituted laws governing power plant siting.

[17]Based on retail prices reported in Energy Information Administration (EIA), Monthly Energy Review, January 1995, Table 9.9 (Prices adjusted for inflation using the GDP Deflator (1987 = 100)).

[18]*Id.*

Policies Act of 1978 (PURPA) (discussed infra), also prompted some industrial customers to bypass utilities by constructing their own generation facilities. This further exacerbated rate increases for remaining customers -- primarily residential and commercial customers.

Consumers responded to these "rate shocks" by exerting pressure on regulatory bodies to investigate the prudence of management decisions to build generating plants, especially when construction resulted in cost overruns, excess capacity, or both. Between 1985 and 1992, writeoffs of nuclear power plants totalled $22.4 billion.[19] These writeoffs significantly reduced the earnings of the affected utilities.[20] Delays in obtaining rate increases to reflect the effects of inflation further reduced investor returns. Thus, many utilities became reluctant to commit capital to long-term construction decisions involving large scale generating plants.[21]

In addition to economic changes in the industry, significant technological changes in both generation and transmission have occurred since 1935. Through the 1960s, bigger was cheaper in the generation sector and the industry was able to capitalize on economies of scale to produce power

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[19]*See* Black & Pierce, *supra* at p. 1346 (These writeoffs were "about 17% of the book value of total 1992 utility investment.").

[20]*Id.*

[21]*Id.* ("The high perceived risk of future disallowances reversed utilities' incentives to overinvest, and made utilities extremely reluctant to build new power plants.").

at lower per-unit costs from larger and larger plants.[22] As a result, large utility companies that could finance and manage construction projects of larger scale had a price advantage over smaller utility companies and customers who might otherwise have considered building their own generating units. Scale economies encouraged power generation by large vertically-integrated utility companies that also transmitted and distributed power. Beginning in the 1970s, however, additional economies of scale in generation were no longer being achieved.[23] A significant factor was that larger generation units were found to need relatively greater maintenance and experience longer downtimes.[24] The electric **[31,641]** industry faced the situation "where the price of each incremental unit of electric power exceeded the average cost."[25] Bigger was no longer better.

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[22]*See* Preston Michie, Billing Credits for Conservation, Renewable, and Other Electric Power Resources: an Alternative to Marginal-Cost-Based Power Rates in the Pacific Northwest, 13 Environmental Law 963, 964-65 (1983).

[23]*Id.* at p. 965.

[24]Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 37 ("As larger units were constructed, however, utilities discovered that downtime was as much as 5 times greater for units larger than 600 megawatts than for units in the 100-megawatt range.")

[25]*Id.*; *see also* George A. Perrault, Downsizing Generation: Utility Plans for the 1990s, Pub. Util. Fort. 15-16 (Sept. 27, 1990) ("The large base-load generating units that form the backbone of utility systems are almost totally absent from capacity plans for the 1990s.").

Further dictating against larger generation units were advances in technologies that allowed scale economies to be exploited by smaller size units, thereby allowing smaller new plants to be brought on line at costs below those of the large plants of the 1970s and earlier. Such new technologies include combined cycle units and conventional steam units that use circulating fluidized bed boilers.[26]

The combined cycle generating plants generally use natural gas as their primary fuel. This technology has been made possible by the development of more efficient gas turbines, shorter construction lead times, lower capital costs, increased reliability, and relatively minimal environmental impacts.[27] Similarly, the circulating fluidized bed combustion boilers, fueled by coal and other conventional fuels, provide a more efficient and less polluting resource.

Today, "the optimum size (of generation plants) has shifted from (more than 500 MW) (10-year lead time) to smaller units (one-year lead time) (in the 50- to 150-MW

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[26]"From 1982 through 1991, the average capacity of fluidized-bed units increased rapidly to 72 megawatts for 4 units in 1991. The average capacity for the 19 units planned to begin operating in 1992 through 1995 increases to 83 megawatts." Energy Information Administration, *The Changing Structure of the Electric Power Industry 1970-1991* (March 1993) 38.

[27]*See* Charles E. Bayless, Less is More: Why Gas Turbines Will Transform Electric Utilities, Pub. Util. Fort. (Dec. 1, 1994) 21.

range)."[28] Indeed, smaller and more efficient gas-fired combined-cycle generation facilities can produce power on the grid at a cost ranging from 5 cents per kWh to less than 3 cents per kWh.[29] This is significantly less than the costs for large plants constructed and installed by utilities over the last decade, which were typically in the range of 4 to 7 cents per kWh for coal plants and 9 to 15 cents for nuclear plants.[30] Significant changes have also occurred in the transmission sector of the industry. Technological advances in transmission have made possible the economic transmission of electric power over long distances at higher voltages.[31] This has made

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[28]*Id.* at p. 24. *See also* Wallace E. Brand, Is Bigger Better? Market Power in Bulk Power Supply: From FDR to NOPR, Pub. Util. Fort. (Feb. 15, 1996) 23 at p. 25 (while the optimal baseload unit size is about 500 MW for coal-fired steam turbines, the optimal size for gas fired combined-cycle units is about 150 to 200 MW).

[29]FERC staff calculations based in part on combined-cycle plant cost data reported in 1994 FERC Form No. 1 for a sample of units placed in service during 1990-94. Costs vary with regional fuel and construction costs, among other reasons.

[30]Coal and Nuclear plant cost data reported in 1994 FERC Form No. 1 and the EIA report, *Electric Plant Cost and Power Production Expenses 1991*, 1993 DOE/EIA-0455(91), for plants placed in service during 1986-94; *see also* The 1994 Electric Executives' Forum, Bakke (President and CEO of the AES Corporation), Pub. Util. Fort. (June 1, 1994) 45 ("New generation can be built at about 3 cents per kilowatt-hour (U.S. average). Old generation costs about twice that * * *").

[31]*See* Black & Pierce, *supra* at p. 1345 (In the late 1960s and 1970s, improved transmission efficiency and development of

it technically feasible for utilities with lower cost generation sources to reach previously isolated systems where customers had been captive to higher cost generation. In addition, the nature and magnitude of coordination transactions[32] have changed dramatically since enactment of the FPA, allowing increased coordinated operations and reduced reserve margins. Substantial amounts of electricity now move between regions, as well as between utilities in the same region. Physically isolated systems have become a thing of the past.

[31,642]

C. *The Public Utility Regulatory Policies Act and the Growth of Competition*

In enacting PURPA,[33] Congress recognized that the rising costs and decreasing efficiencies of utility-owned generating facilities were increasing rates and harming the

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regional transmission networks "made it possible to build power plants up to 1000 miles from power users.").

[32]Coordination transactions are voluntary sales or exchanges of specialized electricity services that allow buyers to realize cost savings or reliability gains that are not attainable if they rely solely on their own resources. For sellers, these transactions provide opportunities to earn additional revenue, and to lower customer rates, from capacity that is temporarily excess to native load capacity requirements.

[33]Pub. L. No. 95-617, 92 Stat. 3117 (codified in U.S.C. sections 15, 16, 26, 30, 42, and 43).

economy as a whole.[34] To lessen dependence on expensive foreign oil, avoid repetition of the 1977 natural gas shortage, and control consumer costs, Congress sought to encourage electric utilities to conserve oil and natural gas.[35] In particular, Congress sanctioned the development of alternative generation sources designated as "qualifying facilities" (QFs) as a means of reducing the demand for traditional fossil fuels.[36] PURPA required utilities to purchase power from QFs

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[34]*See generally FERC v. Mississippi*, 456 U.S. 742, 745-46 (1982).

[35]The Power Plant and Industrial Fuel Use Act of 1978. Pub. L. No. 95-617, 92 Stat. 3117 (codified in U.S.C. sections 15, 16, 26, 30, 42, and 43).

[36]QFs include certain cogenerators and small power producers. PURPA also added sections 210, 211, and 212 to the FPA, providing the Commission with authority to approve applications for interconnections and, in limited circumstances, wheeling. However, under section 211, as enacted in PURPA, the Commission could approve an application for wheeling only if it found, inter alia, that the order "would reasonably preserve existing competitive relationships." Because of this and other limitations in sections 211 and 212 as originally enacted, the provision was virtually ineffective. Only one section 211 order was ever issued pursuant to the original provision, and it was pursuant to a settlement. *See Public Service Company of Oklahoma*, 38 FERC ¶61,050 (1987). As discussed *infra*, section 211 was subsequently revised by the Energy Policy Act of 1992.

at a price not to exceed the utility's avoided costs and to sell backup power to QFs.[37]

PURPA specifically set forth limitations on who, and what, could qualify as QFs. In addition to technological and size criteria, PURPA set limits on who could own QFs.[38] Notwithstanding these limitations, QFs proliferated. In 1989, there were 576 QF facilities. By 1993, there were more than 1,200 such facilities.[39] For the same time period, installed QF capacity increased from 27,429 megawatts to 47,774 megawatts.[40] The rapid expansion and performance of the QF industry demonstrated that traditional, vertically integrated public utilities need not be the only sources of reliable power.

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[37]456 U.S. at p. 750. Congress recognized that encouragement was needed in part because utilities had been reluctant to purchase electric power from, and sell power to, nonutility generators. *Id.* at pp. 750-51.

[38]For example, PURPA provided that a cogeneration facility or small power production facility could not be owned by a person primarily engaged in the generation or sale of electric power (other than from cogeneration or small power production facilities). *See* 16 U.S.C.

[39]Energy Information Administration, *Electric Power Annual 1993* (December 1994) 124 (Table 77).

[40]*Id.* EIA data for 1989 through 1991 was for facilities of 5 megawatts or more and for 1992 and 1993 was for facilities of 1 megawatt or more. A comparison with Table 74 on page 121 for the years 1992 and 1993 reveals that this mixing of data bases is likely of minimal effect.

During this period, the profile of generation investment began to change, and a market for non-traditional power supply beyond the purchases required by PURPA began to emerge. QFs were limited to cogenerators and small power producers.[41]

However, other non-traditional power producers who could not meet the QF criteria began to build new capacity to compete in bulk power markets, without such PURPA benefits as the mandatory purchase requirements. These producers, known as independent power producers (IPPs), were predominantly single-asset generation companies that did not own any transmission or distribution facilities. While traditional utilities were generally **[31,643]** reluctant at that time to invest in new generating facilities under cost of service regulation, utilities increasingly became interested in participating in this new generation sector. They organized affiliated power producers (APPs), with assets not included in utility rate base, and sought to sell power in their own service territories and the territories of other utilities. At the same

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[41]Generally, the law has imposed an 80 MW cap on small power producers. A limited exception enacted in 1990 permitted small power facilities that could exceed 80 MW and still qualify as QFs under PURPA. This exception was limited to certain solar, wind, waste, and geothermal small power production facilities and only covered applications for certification of facilities as qualifying small power production facilities that were submitted no later than December 31, 1994 and for which construction commences no later than December 31, 1999. See Solar, Wind, Waste, and Geothermal Power Production Incentives Act of 1990, Pub. L. No. 101-575, 104 Stat. 2834 (1990), *amended*, Pub. L. No. 102-46, 105 Stat. 249 (1991).

time, power marketers arose. These entities -- owning no transmission or generation -- buy and sell power.[42]

There were two major impediments to the development of IPPs and APPs. First, the ownership restrictions of the Public Utility Holding Company Act (PUHCA)[43] severely inhibited these new entities from entering the generation business.[44] Second, these entities needed transmission service in order to compete in electricity markets.

While the Commission had no authority to remove PUHCA restrictions,[45] it encouraged the development of IPPs and APPs, as well as emerging power marketers, by authorizing market-based rates for their power sales on a case-by-case basis and by encouraging more widely available transmission access. From 1989 through 1993, facilities owned by IPPs and other non-traditional generators (other

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[42]The first power marketer in the electric industry was Citizens Energy Corporation. *See Citizens Energy Corporation*, 35 FERC ¶61,198 (1986). Power marketers take title to electric energy. Power brokers, on the other hand, do not take title and are limited to a matchmaking role.

[43]15 U.S.C. §79 *et seq.*

[44]As discussed *infra*, Congress eventually provided a means to avoid the PUHCA restrictions by creating exempt wholesale generators (EWGs) in the Energy Policy Act.

[45]The industry was successful to some extent in developing ownership structures that permitted such investment. *See, e.g., Commonwealth Atlantic Limited Partnership*, 51 FERC ¶61,368 at p. 62,240 and n.20 (1990).

than QFs) increased from 249 to 634 and their installed capacity increased from 9,216 megawatts to 13,004 megawatts.[46] Indeed, "[i]n 1992, for the first time, generating capacity added by independent producers exceeded capacity added by utilities."[47]

Market-based rates helped to develop competitive bulk power markets. A generating utility allowed to sell its power at market-based rates could move more quickly to take advantage of short-term or even long-term market opportunities than those laboring under traditional cost-of-service tariffs, which entail procedural delays in achieving tariff approvals and changes.

In approving these market-based rates, the Commission required, inter alia, that the seller and any of its affiliates lack market power or mitigate any market power that they may have possessed.[48] The major concern of the Commission was whether the seller or its affiliates could limit competition and thereby drive up prices. A key inquiry

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[46]Energy Information Administration, *Electric Power Annual 1993* (December 1994) 124 (Table 77).

[47]Black & Pierce, *supra* at p. 1349 n.25.

[48]*See, e.g., Ocean State Power*, 44 FERC ¶61,261 (1988); *Commonwealth Atlantic Limited Partnership*, 51 FERC ¶61,368 (1990); *Citizens Power & Light Company*, 48 FERC ¶61,210 (1989); *Orange and Rockland Utilities, Inc.*, 42 FERC ¶61,012 (1988); *Doswell Limited Partnership*, 50 FERC ¶61,251 (1990) (Doswell); and *Dartmouth Power Associates Limited Partnership*, 53 FERC ¶61,117 (1990).

became whether the seller or its affiliates owned or controlled transmission facilities in the relevant service area and therefore, by denying access or imposing discriminatory terms or conditions on transmission service, could foreclose other generators from competing.[49] As we have previously explained:

> The most likely route to market power in today's electric utility industry lies through ownership or control of transmission facilities. Usually, the source of market power is dominant or exclusive ownership of the facilities. However, market power also may be gained without ownership. Contracts can confer the same rights of control. Entities with contractual control over transmission facilities can withhold supply and extract monopoly prices just as effectively as those who control facilities through ownership.[50]

As entry into wholesale power generation markets increased, the ability of customers to gain access to the transmission services necessary to reach competing **[31,644]**

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[49] *See, e.g., Doswell,* 50 FERC at p. 61,757.

[50] *Citizens Power & Light Corporation*, 48 FERC ¶61,210 at p. 61,777 (1989) (emphasis in original); *see also Utah Power & Light Company, PacifiCorp and PC/UP&L Merging Corporation*, 45 FERC ¶61,095 at pp. 61,287-89 (1988), *order on reh'g*, 47 FERC ¶61,209, *order on reh'g*, 48 FERC ¶61,035 (1989), *remanded in part sub nom. Environmental Action, Inc. v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991), *order on remand*, 57 FERC ¶61,363 (1991).

suppliers became increasingly important.[51] In addition, beginning in the late 1980s, in order to mitigate their market power to meet Commission conditions, public utilities seeking Commission approval of mergers or consolidations under section 203 of the FPA or Commission authorization for blanket approval of market-based rates for generation services under section 205 of the FPA, filed "open access" transmission tariffs of general applicability.[52] The

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[51]In earlier years, a few customers were able to obtain access as a result of litigation, beginning with the Supreme Court's decision in *Otter Tail Power Company v. United States*, 410 U.S. 366 (1973). Additionally, some customers gained access by virtue of Nuclear Regulatory Commission license conditions and voluntary preference power transmission arrangements associated with federal power marketing agencies. *See, e.g., Consumers Power Company*, 6 NRC 887, 1036-44 (1977) and *The Toledo Edison Company and Cleveland Electric Illuminating Company*, 10 NRC 265, 327-34 (1979). *See Florida Municipal Power Agency v. Florida Power and Light Company*, 839 F. Supp. 1563 (M.D. Fla. 1993). *See also* Electricity Transmission: Realities, Theory and Policy Alternatives, The Transmission Task Force Report to the Commission, October 1989, 197.

[52]*See, e.g., Public Service Company of Colorado*, 59 FERC ¶61,311 (1992), *reh'g denied*, 62 FERC ¶61,013 (1993); *Utah Power & Light Company, et al.*, Opinion No. 318, 45 FERC ¶61,095 (1988), *order on reh'g*, Opinion No. 318-A, 47 FERC ¶61,209 (1989), *order on reh'g*, Opinion No. 318-B, 48 FERC ¶61,035 (1989), *aff'd in relevant part sub nom. Environmental Action Inc. v. FERC*, 939 F.2d 1057 (D.C. Cir. 1991); *Northeast Utilities Service Company (Public Service Company of New Hampshire)*, Opinion No. 364-A, 58 FERC ¶61,070, *reh'g denied*, Opinion No. 364-B, 59 FERC ¶61,042, *order granting motion to*

Commission applied its market rate analysis to IOUs, as well as IPPs, APPs, and marketers, and allowed IOUs to sell at market-based rates only if they opened their transmission systems to competitors.[53] The Commission also approved proposed mergers on the condition that the merging companies remedy anticompetitive effects potentially caused by the merger by filing "open access" tariffs. These early "open access" tariffs required only that the companies provide point-to-point transmission services, which is a much narrower requirement than that being imposed in this Rule and did not require transmission owners to provide to others the same quality of service that they themselves enjoyed.

Following PURPA, the economic and technological changes in the transmission and generation sectors helped give impetus to the many new entrants in the generating markets who could sell electric energy profitably with smaller scale technology at a lower price than many utilities selling from their existing generation facilities at rates reflecting cost. However, it became increasingly clear that the potential consumer benefits that could be derived from these technological advances could be realized only if more efficient generating plants could obtain access to the regional transmission grids. Because many traditional vertically

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vacate and dismissing request for rehearing, 59 FERC ¶61,089 (1992), *affirmed in relevant part sub nom. Northeast Utilities Service Company v. FERC*, 993 F.2d 937 (1st Cir. 1993).

[53]*See, e.g., Public Service of Indiana, Inc.*, 51 FERC ¶61,367 (1990), *reh'g denied*, 52 FERC ¶61,260 (1990), *appeal dismissed sub nom. Northern Indiana Public Service Company v. FERC*, 954 F.2d 736 (D.C.Cir. 1992).

integrated utilities still did not provide open access to third parties and still favored their own generation if and when they provided transmission access to third parties, barriers continued to exist to cheaper, more efficient generation sources.

D. *The Energy Policy Act*

In response to the competitive developments following PURPA, and the fact that PUHCA and lack of transmission access remained major barriers to new generators, Congress enacted Title VII of the Energy Policy Act of 1992 (Energy Policy Act).[54] A goal of the Energy Policy Act was to promote greater competition in bulk power markets by encouraging new generation entrants, known as exempt wholesale generators (EWGs), and **[31,645]** by expanding the Commission's authority under sections 211 and 212 of the FPA to approve applications for transmission services.[55]

An EWG is defined as

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[54]Pub. L. No. 102-486, 106 Stat. 2776 (1992), codified at, among other places, 15 U.S.C. §79z-5a and 16 U.S.C. §796(22-25), 824j-l.

[55]*See El Paso Electric Company and Central and South West Services Inc.*, 68 FERC ¶61,181 at p. 61,914 (1994) (CSW); *see also* Paul Kemezis, FERC's Competitive Muscle: The Comparability Standard, Electrical World 45 (Jan. 1995) ("In EPAct, Congress made it clear that the electric-power industry was to move toward a fully competitive market system, but left most of the implementation to FERC.").

Any person determined by the Federal Energy Regulatory Commission to be engaged directly, or indirectly through one or more affiliates as defined in [PUHCA] section 2(a)(11)(B), and exclusively in the business of owning or operating, or both owning and operating, all or part of one or more eligible facilities and selling electric energy at wholesale.[56]

If the Commission, upon an application, determines that a person is an EWG, that person will be exempt from PUHCA.[57] This provision removed a significant impediment to the development of IPPs and APPs by allowing them to develop projects as EWGs free from the strictures of PUHCA or the QF PURPA limitations.

While sections 211 and 212, as enacted by PURPA, were intended to provide greater access to the transmission grid, the limitations placed on these sections made them unusable in virtually all circumstances.[58] However, as amended by the Energy Policy Act, these sections now give the Commission broader authority to order transmitting utilities to provide wholesale transmission services, upon application, to any electric utility, Federal power marketing agency, or any other person generating electric energy for sale for resale.

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[56]15 U.S.C. §79z-5a.

[57]15 U.S.C. §79z-5a(e).

[58]*See supra* note 36.

The Energy Policy Act also added section 213 to the FPA. Section 213(a) requires a transmitting utility that does not agree to provide wholesale transmission service in accordance with a good faith request to provide a written explanation of its proposed rates, terms, and conditions and its analysis of any physical or other constraints.[59] Section 213(b) required the Commission to enact a rule requiring transmitting utilities to submit annual information concerning potentially available transmission capacity and known constraints.[60]

E. *The Present Competitive Environment*

Following the Energy Policy Act, the Commission established rules: (1) for certain generators to obtain EWG

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[59]*See* Policy Statement Regarding Good Faith Requests for Transmission Services and Responses by Transmitting Utilities Under Sections 211(a) and 213(a) of the Federal Power Act, as Amended and Added by the Energy Policy Act of 1992, 58 FR 38964 (July 21, 1993), FERC Statutes and Regulations ¶30,975 (1993) (Policy Statement Regarding Good Faith Requests for Transmission Services).

[60]*See* New Reporting Requirements Implementing Section 213(b) of the Federal Power Act and Supporting Expanded Regulatory Responsibilities Under the Energy Policy Act of 1992, and Conforming and Other Changes to Form No. FERC-714, 58 FR 52420 (October 8, 1993), FERC *Statutes and Regulations* ¶30,980 (Order No. 558), *reh'g denied*, Order No. 558-A, 65 FERC ¶61,324 (1993), *regulations modified*, 59 FR 15333 (April 1, 1994), FERC *Statutes and Regulations* ¶30,993.

status and thus an exemption from PUHCA;[61] and (2) that required transmission information availability. The Commission also pursued a number of initiatives aimed at fostering the development of more competitive bulk power markets, including aggressive implementation of section 211, a new look at undue discrimination under the FPA, easing of market entry for sellers of generation from new facilities, and initiation of a number of industry-wide reforms. As stated by the Commission, in recognition of the Congressional goal in **[31,646]** the Energy Policy Act of creating competitive bulk power markets:

Our goal is to facilitate the development of competitively priced generation supply options, and to ensure that wholesale purchasers of electric energy can reach alternative power suppliers and vice versa.[62]

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[61] *See* Order No. 550, Filing Requirements and Ministerial Procedures for Persons Seeking Exempt Wholesale Generator Status, 58 FR 8897 (February 18, 1993), *FERC Statute and Regulations* ¶30,964, *order on reh'g*, Order No. 550-A, 58 FR 21250 (April 20, 1993), *FERC Statutes and Regulations* ¶30,969 (1993). As recognized by Congress and the Commission, availability of transmission information is critical in developing competitive markets. *See supra* notes 59 and 60. This opened the "black box" of information that previously was available only to transmission owners.

[62] *See* Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, Notice of Proposed Rulemaking, 59 FR 35274 (July 11, 1994), FERC *Statutes and Regulations* ¶32,507 at p. 32,866 (Stranded Cost NOPR); *American Electric Power Service Corporation*, 67 FERC ¶61,168, *clarified*, 67 FERC ¶61,317 (1994).

1. Use of Sections 211 and 212 to Obtain Transmission Access

The Commission has aggressively implemented sections 211 and 212 of the FPA, as amended by the Energy Policy Act, in order to promote competitive markets.[63] When wheeling requests under sections 211 and 212 have been made, the Commission has required wheeling in almost all of the requests it has processed. To date, the Commission has issued orders (proposed or final) requiring wheeling in 12 of the 14 cases it has acted on.[64]

As a general matter, section 211 has permitted some inroads to be made by customers in obtaining transmission service from public utilities that historically have declined to provide access to their systems, or have offered service only on a discriminatory basis. Under section 211, the Commission has granted requests for the broader type of service that most utilities historically have refused to provide -- network service. Although transmission owners have provided limited amounts of unbundled point-to-point transmission service, third- party customers have not been able to obtain the flexibility of service that transmission owners enjoy.

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[63]16 U.S.C.A. §§824j-824k (West 1985 and Supp. 1994).

[64]*See, e.g.*, final orders issued in *City of Bedford*, 68 FERC ¶61,003 (1994), *reh'g denied*, 73 FERC ¶61,322 (1995); *Florida Municipal Power Agency v. Florida Power & Light Company*, 67 FERC ¶61,167 (1994), *order on reh'g*, 74 FERC ¶61,006 (1996); *Minnesota Municipal Power Agency*, 68 FERC ¶61,060 (1994); and *Tex-La Electric Cooperative of Texas*, 69 FERC ¶61,269 (1994); *see also* Appendix A.

In Florida Municipal, a section 211 case, the Commission ordered "network," rather than the narrower "point-to-point," service.[65] Network service permits the applicant to fully integrate load and resources on an instantaneous basis in a manner similar to the transmission owner's integration of its own load and resources. At the same time, the Commission made the generic finding that the availability of transmission service will enhance competition in the market for power supplies and lead to lower costs for consumers. The Commission explained that as long as the transmitting utility is fully and fairly compensated and there is no unreasonable impairment of reliability, transmission service is in the public interest.[66]

As discussed infra, based on the mounting competitive pressures in the industry and rapidly evolving markets, we

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[65]*See Florida Municipal Power Agency v. Florida Power & Light Company*, 65 FERC ¶61,125, *reh'g dismissed*, 65 FERC ¶61,372 (1993), *final order*, 67 FERC ¶61,167 (1994), *order on reh'g*, 74 FERC ¶61,006 (1996). The Commission has "characterized point-to-point service as involving designated points of entry into and exit from the transmitting utility's system, with a designated amount of transfer capability at each point." *El Paso Electric Company v. Southwestern Public Service Company*, 68 FERC ¶61,182 at p. 61,926 n.9 (1994) (*citing Entergy Services, Inc.*, 58 FERC ¶61,234 at p. 61,768 (1993), *reh'g dismissed*, 68 FERC ¶61,399 (1994)). Network service allows more flexibility by allowing a transmission customer to use the entire transmission network to provide generation service for specified resources and specified loads without having to pay multiple charges for each resource-load pairing.

[66]*Florida Municipal*, 67 FERC at p. 61,477.

have concluded that section 211 alone is not enough to eliminate undue discrimination. The comments received on the proposed rules, discussed in detail infra, confirm this conclusion. The significant time delays involved in filing an individual service request for bilateral service under section 211 place the customer at a severe disadvantage compared to the transmission owner and can result in discriminatory treatment in the use of the transmission system. It is an inadequate procedural substitute for readily available service under a filed non-discriminatory open access tariff. As the Commission noted in Hermiston Generating Company, **[31,647]** "[t]he ability to spend time and resources litigating the rates, terms and conditions of transmission access is not equivalent to an enforceable voluntary offer to provide comparable service under known rates, terms and conditions."[67]

2. Commission's Comparability Standard

In the Spring of 1994, the Commission began to address the problem of the disparity in transmission service that utilities provided to third parties in comparison to their own uses of the transmission system. In the seminal case in this area, American Electric Power Service Corporation (AEP), the company voluntarily proposed a tariff of general applicability that would offer firm, point-to-point transmission

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[67]69 FERC ¶61,035 at p. 61,165 (1994), *reh'g denied*, 72 FERC ¶61,071 (1995); *see also Southwest Regional Transmission Association*, 69 FERC ¶61,100 at p. 61,398 (1994), *order on compliance filing*, 73 FERC ¶61,147 (1995) *(SWRTA)*.

service for a minimum of one month.[68] The Commission accepted the proposed transmission tariff for filing and suspended its effectiveness for one day, subject to refund.[69] Rehearing requests challenged the Commission's summary approval of the restriction of service to point-to-point as being discriminatory and anticompetitive.[70] The rehearing requests argued that the tariff should be expanded to include network services such as those used by the transmission owner. On rehearing, the Commission announced a new standard for evaluating claims of undue discrimination.

The Commission found that a voluntarily offered, new open access transmission tariff that did not provide for services comparable to those that the transmission owner provided itself was unduly discriminatory and anticompetitive.[71] In reaching that conclusion, the

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[68]64 FERC 61,279 (1993), *reh'g granted*, 67 FERC ¶61,168, *clarified*, 67 FERC ¶61,317 (1994).

[69]The Commission explained that AEP could limit the service it was offering because it was "providing the service voluntarily under a tariff of general applicability." 64 FERC at p. 62,978.

[70]*AEP*, 67 FERC at p. 61,489.

[71]With respect to anticompetitive effects, the Commission explained that it has "adhered to the Supreme Court's determination that the Commission's 'important and broad regulatory power * * * carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to sections 202 and 203, and under like directives contained in sections 205, 206 and 207.' *Gulf*

Commission broadened its undue discrimination analysis (which traditionally had focused on the rates, terms, and conditions faced by similarly situated third- party customers) to include a focus on the rates, terms, and conditions of a utility's own uses of the transmission system:

> (A)n open access tariff that is not unduly discriminatory or anticompetitive should offer third parties access on the same or comparable basis, and under the same or comparable terms and conditions, as the transmission provider's uses of its system.[72]

Refocusing the analysis was necessitated by the changing conditions in the electric utility industry, including the emergence of non-traditional suppliers and greater competition in bulk power markets. Because a transmission provider may use its system in different ways (e.g., to integrate load and resources when serving retail native load, to make off-system sales or purchases, or to serve wholesale requirements customers), the Commission set for hearing the factual issues associated with identifying those uses, as well as any potential impediments or consequences to providing comparable services to third parties.[73]

States Utilities Company v. FPC, 411 U.S. 747, 758-59 (1972)." *Id.* at p. 61,490 (footnote omitted). The Commission reaffirmed that it would examine how best to fulfill this responsibility, as well as its responsibility to prevent undue discrimination, in light of the changing conditions in the electric utility industry. *Id.*

[72] *Id.* at p. 61,490.

[73] *Id.* at pp. 61,490-91.

After AEP, the Commission applied this comparability standard to a proposed open access transmission tariff that was filed by Kansas City Power & Light Company (KCP&L) in support of a proposal to sell generation at market-based rates.[74] The Commission explained that, in light of AEP, the utility's proposed open access transmission tariff (which provided only **[31,648]** for point-to-point service) did not adequately mitigate its transmission market power so as to justify allowing the requested market-based rates. KCP&L could charge market-based rates for sales only if it modified its proposed transmission tariff to reflect the AEP comparability standard.

Since then, the Commission has required comparable service in a variety of contexts, and has set for hearing the factual issues associated with comparable service. For example, the Commission found that market power can be adequately mitigated only if a merged company offers transmission services in accordance with the AEP comparability standard.[75] The Commission further held that, even if a merger does not result in an increase in market power, the merger would not be consistent with the public interest under section 203 of the FPA unless the merged company offers comparable transmission services, as defined in AEP.[76] The Commission therefore announced a transmission comparability requirement for all new mergers:

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[74]*See Kansas City Power & Light Company*, 67 FERC ¶61,183 (1994), *reh'g pending*.

[75]*E.g.*, *CSW*, *supra*, 68 FERC at p. 61,914.

[76]*Id.*

Given the transition of the electric utility industry as a whole, we conclude that, absent other compelling public interest considerations, coordination in the public interest can best be secured only if merging utilities offer comparable transmission services.[77]

In Heartland Energy Services, Inc.,[78] the Commission applied its comparability standard to an affiliated electric power marketer seeking blanket authorization to sell electricity at market-based rates. The Commission explained that

For all future cases involving blanket approval of market-based rates an offer of comparable transmission services will be required before the Commission will be able to find that transmission market power has been adequately mitigated. In the context of an affiliated power marketer, this means that all of its affiliated utilities must have a comparable transmission tariff on file.[79]

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[77] *Id.* at p. 61,915 (footnote omitted).

[78] 68 FERC ¶61,223 (1994).

[79] *Id.* at p. 62,060. In *InterCoast Power Marketing Company*, 68 FERC ¶61,248, *clarified*, 68 FERC ¶61,324 (1994), the Commission rejected an affiliated marketer's proposal to sell at market rates without its affiliate utility offering comparable transmission services. The Commission stated that the only way to ensure that InterCoast does not have transmission market power is to require its affiliated public utility to offer comparable transmission services. *See also LG&E Power Marketing Inc.*, 68 FERC ¶61,247 at pp. 62,120-21 (1994). The Commission added

The Commission also denied a request by a company affiliated with a transmission-owning utility seeking permission to sell power at market-based rates to a particular customer. The denial was without prejudice to refiling such a request in a new section 205 proceeding, but only after the affiliated transmission-owning utility filed a comparable transmission service tariff.[80] The Commission added that it

> Will require comparability in any situation in which a seller seeking market-based rates is affiliated with an owner or controller of transmission facilities.[81]

The Commission has also stated that "it will henceforth apply the transmission comparability standard announced in the AEP case to all transmitting utility members of an RTG."[82]

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that this is consistent with encouraging competitive bulk power markets as envisioned by the Energy Policy Act of 1992. *Id.* at p. 62,132.

[80]*See Hermiston Generating Company*, 69 FERC ¶61,035 at p. 61,164 (1994), *reh'g pending*. The Commission subsequently accepted the rates on a cost basis. See Letter Order dated November 10, 1994.

[81]*Id.* at p. 61,165.

[82]*See SWRTA*, 69 FERC at p. 61,397; *see also PacifiCorp, the California Municipal Utilities Association, and the Independent Energy Producers (on behalf of Western Regional Transmission Association)*, 69 FERC ¶61,099, *order on reh'g*, 69 FERC ¶61,352 (1994), *order on compliance filing*, 71 FERC ¶61,158 (1995) (*WRTA*). An RTG is a regional transmission group. It is defined as

[31,649]

The Commission further declared that comparable services must be provided through "open access" tariffs rather than only on a contract-by-contract basis:

(T)ariffs are essential to the provision of comparable services. Tariffs set out the services that are available and the terms and conditions under which those services will be made available * * *. (In contrast), a negotiation process creates uncertainty- and imposes on customers delay and other transaction costs that the transmitting utility members of an RTG do not incur when using the transmission for their own benefit. Moreover, the ability to execute separate transmission agreements with different but similarly situated customers is the ability to unduly discriminate among them. A tariff ensures against such discrimination in the RTG.[83]

Thus, the Commission required the RTGs to amend their bylaws to commit all transmitting utility members to offer comparable transmission services to other RTG members pursuant to a transmission tariff or tariffs.

As discussed below, since the AEP comparability standard was announced, the Commission has set for hearing

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"a voluntary organization of transmission owners, transmission users, and other entities interested in coordinating transmission planning (and expansion), operation and use on a regional (and inter- regional." Policy Statement Regarding Regional Transmission Groups, 58 FR 41626 (August 5, 1993), *FERC Statutes and Regulations* ¶30,976, at p. 30,870 n.4 (RTG Policy Statement).

[83]*SWRTA*, 69 FERC at p. 61,398.

44 open access tariffs to determine what constitutes comparable service. This number includes tariffs filed subsequent to the Open Access NOPR. All tariffs have now been made subject to the outcome of the Final Rule.

3. Lack of Market Power in New Generation

In 1994 in the KCP&L case, discussed in the prior section, the Commission continued to recognize that transmission remains a natural monopoly. However, it found that, in light of the industry and statutory changes that now allow ease of market entry, no wholesale seller of generation has market power in generation from new facilities.[84] In particular, the Commission explained that it had previously noted in Entergy Services, Inc. that

There was significant evidence that non-traditional power project developers, including qualifying facilities and independent power projects, are becoming viable competitors in long-run markets.[85]

The Commission further explained that since Entergy, Congress had enacted the Energy Policy Act, which had lowered barriers to the entry of new suppliers by creating a new class of power suppliers -- EWGs -- that are exempt from

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[84] *KCP&L*, 67 FERC ¶61,183 (1994).

[85] *Id.* at p. 61,557 (citing *Entergy Services, Inc.*, 58 FERC ¶61,234 at p. 61,756 and nn.63 and 65 (*Entergy*)).

the provisions of PUHCA.[86] The Commission concluded that, in considering market-based rate proposals for generation sales, it need only focus on market power in transmission, generation market power in short-run markets, and other barriers to entry.[87]

4. Further Commission Action Addressing a More Competitive Electric Industry

To address the fact that the electric industry is becoming more competitive, and to remove barriers that might inhibit a more competitive industry, the Commission has initiated a number of proceedings: (1) Stranded Cost NOPR,[88] (2) Transmission Pricing Policy Statement,[89] (3) Pooling Notice of Inquiry,[90] (4) Regional Transmission Group

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[86]*Id.* The Commission added that "after examining generation dominance in many different cases over the years, we have yet to find an instance of generation dominance in long-run bulk power markets." *Id.*

[87]*Id.*

[88]*FERC Statutes and Regulations* ¶32,507 (1994).

[89]Inquiry Concerning the Commission's Pricing Policy for Transmission Services Provided by Public Utilities Under the Federal Power Act, 59 FR 55031 (November 3, 1994), *FERC Statutes and Regulations* ¶31,005 (Transmission Pricing Policy Statement).

[90]Inquiry Concerning Alternative Power Pooling Institutions Under the Federal Power Act, 59 FR 54851 (October 26, 1994), *FERC Statutes and Regulations* ¶35,529 (1995) (Pooling Notice of

(RTG) Policy Statement,[91] and (5) Notice of Inquiry on Merger Policy.[92]

In the Stranded Cost NOPR the Commission recognized that the trend toward greater transmission access and the transition **[31,650]** to a fully competitive bulk power market could cause some utilities to incur stranded costs as wholesale requirements customers (or retail customers) use their supplier's transmission to purchase power elsewhere. As the Commission noted, a utility may have built facilities or entered into long-term fuel or purchased power supply contracts with the reasonable expectation that its customers would renew their contracts and would pay their share of long-term investments and other incurred costs. If the customer obtains another power supplier, the utility may have stranded costs. If the utility cannot locate an alternative buyer or somehow mitigate the stranded costs, the Commission explained that "the costs must be recovered from either the departing customer or the remaining customers or borne by the utility's shareholders."[93] Accordingly, the Commission proposed to establish provisions concerning the recovery of wholesale and retail stranded costs by public utilities and transmitting utilities.

Inquiry).

[91]*FERC Statutes and Regulations* ¶30,976 (RTG Policy Statement).

[92]*FERC Statutes and Regulations* ¶35,531 (1996).

[93]*FERC Statutes and Regulations* ¶32,507 at p. 32,864.

In the Transmission Pricing Policy Statement, the Commission announced a new policy providing greater flexibility in the pricing of transmission services provided by public utilities and transmitting utilities. The Commission traditionally had allowed only postage-stamp, contract-path pricing.[94] Under the new policy, we will permit a variety of proposals, including distance sensitive and flow-based pricing, which may be more suitable for competitive wholesale power markets.[95] The Commission explained that this "(g)reater pricing flexibility is appropriate in light of the significant competitive changes occurring in wholesale generation markets, and in light of our expanded wheeling authority

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[94]Most transmission contracts set a single price for energy flow over a utility's transmission system. This single- price policy is called "postage stamp" pricing because the rate does not depend on how far the power moves within a company's transmission system. If power flows through several companies, traditional industry practice is to specify that power flows along a "contract path" consisting of the transmission-owning utilities between the ultimate receipt and delivery points. *See Indiana Michigan Power Company*, 64 FERC ¶61,184 at p. 62,545 (1993).

[95]Unlike with postage stamp pricing, with distance-sensitive pricing the cost of moving power through a company depends on how far the power moves within the company. In contrast to contract path pricing, flow-based pricing establishes a price based on the costs of the various parallel paths actually used when the power flows. Because flow-based pricing can account for all parallel paths used by the transaction, all transmission owners with facilities on any of the parallel paths could be compensated for the transaction.

under the Energy Policy Act of 1992."[96] However, the Commission explained that any new transmission pricing proposal must meet the Commission's AEP comparability standard. The Commission further explained that comparability of service applies to price as well as to terms and conditions.[97]

The Commission issued the Pooling Notice of Inquiry to receive comments on traditional power pools and on alternative power pooling institutions that are being explored in today's more competitive environment. The Commission expressed concern that

(G)iven the ongoing changes in the competitive environment of the electric utility industry -- in particular, the potential for substantially increased access to transmission -- we must consider whether we are appropriately balancing our dual objectives of promoting coordination and competition.[98]

Accordingly, the Commission explained that it wished to look at alternative power pooling institutions and to re-examine the role of more traditional power pools in today's environment of increased competition. In particular the Commission expressed its intent to ensure that its policies "are

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[96]*FERC Statutes and Regulations* ¶31,005 at p. 31,136.

[97]*Id.* at p. 31,142.

[98]*FERC Statutes and Regulations* ¶35,529 at p. 35,715.

consistent with the development of a competitive bulk power market."[99]

In the RTG Policy Statement, the Commission announced a policy encouraging the development of RTGs. The Commission explained that a primary purpose of RTGs is to facilitate transmission access for potential users and voluntarily resolve **[31,651]** disputes over such service. The Commission has approved the formation of three RTGs.[100] One of the conditions is that each RTG member must offer comparable transmission services by tariff to other RTG members.

In the merger NOI, the Commission indicated that it will review whether its criteria and policy for evaluating mergers need to be modified in light of the changing circumstances occurring in the electric industry. In addition to the Commission's actions, a number of states have initiated proceedings concerning retail wheeling or proposed legislation for retail wheeling, that is, for ultimate consumers to choose their supplier of power, or other restructuring proposals.[101]

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[99]*Id.* at p. 35,714. As explained below, the Commission held technical conferences on issues surrounding power pools and competition.

[100]*See WRTA* and *SWRTA*, *supra*, and *Northwest Regional Transmission Association*, 71 FERC ¶61,397 (1995).

[101]At least 12 states have retail wheeling proposals, legislation, or pilot programs underway -- Alabama, California, Connecticut, Illinois, Massachusetts, Michigan, New Hampshire, New York, Ohio, Rhode Island, Vermont, and Wisconsin. At least

5. Events Since Issuance of Open Access NOPR

Since issuance of the Open Access NOPR, public utilities have filed, in some form or another, 47 open access tariffs. In acting on those filings, the Commission has made all of the non- rate terms and conditions of those proposed tariffs subject to the outcome of this Final Rule.[102]

Over the last year, the Commission also has received and analyzed more than 20,000 pages of comments that were received from over 400 commenters, as well as additional information provided by industry participants at a number of Commission-initiated technical conferences.[103] Those technical

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14 other states are investigating retail wheeling. Currently, according to a report of the NARUC-affiliated National Council on competition and the Electric Industry, 41 States are actively involved in investigating whether and how to restructure their respective electric power markets. Of this total, 29 State regulatory authorities * * * have initiated investigations. In addition, five State legislatures are involved in similar investigations, while seven other States have joint regulatory/legislative proceedings underway.

Testimony of the Honorable Cheryl L. Parrino, Chair of the Wisconsin Public Service Commission, on behalf of the National Association of Regulatory Utility Commissioners, before the United States Senate Committee on Energy and Natural Resources (March 6, 1996).

[102] *See American Electric Power Service Corporation,* et al., 72 FERC ¶61,287 at p. 61,238 (1995).

[103] Attached to this Final Rule as Appendix B is a list of commenters and the abbreviations used to designate them, including

conferences addressed several issues -- ancillary services, pro forma tariffs, power pools, and ISOs -- and provided significant input to the Commission's formulation of this Final Rule.

F. *Need for Reform*

The many changes discussed above have converged to create a situation in which new generating capacity can be built and operated at prices substantially lower than many utilities' embedded costs of generation. As discussed above, new generation facilities can produce power on the grid at a cost of less than 3 cents per kWh to 5 cents per kWh, yet the costs for large plants constructed and installed over the last decade were typically in the range of 4 to 7 cents per kWh for coal plants and 9 to 15 cents for nuclear plants.

Non-traditional generators are taking advantage of this opportunity to compete. Indeed, the non-traditional generators' share of total U.S. electricity generation increased from 4 percent in 1985 to 10 percent in 1993.[104] Much of this increased share of generation is the result of competitive bidding for new generation resources that has occurred in 37 states. Since 1984, almost 4,000 projects, representing over 400,000 MW, have been offered in response to requests. Over 350 projects have been selected to supply 20,000 MW, and,

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those commenters that filed late.

[104]Energy Information Administration, *Performance Issues for a Changing Electric Power Industry* (January 1995) 10 and (Figure 5).

of these, 126 are now online producing almost 7,800 MW of power.[105]

In addition, the cost of utility-generated electricity differs widely across the major regions of the United States. Average utility rates range from 3 to 5 cents in the Northwest to 9 to 11 cents in California. **[31,652]** Electricity consumers are demanding access to lower cost supplies available in other regions of the United States, and access to the newer, lower cost generation resources. Therefore, it is important that the non-traditional generators of cheaper power be able to gain access to the transmission grid on a non-discriminatory open access basis.

The Commission's goal is to ensure that customers have the benefits of competitively priced generation. However, we must do so without abandoning our traditional obligation to ensure that utilities have a fair opportunity to recover prudently incurred costs and that they maintain power supply reliability. As well, the benefits of competition should not come at the expense of other customers. The Commission believes that requiring utilities to provide non-discriminatory open access transmission tariffs, while simultaneously resolving the extremely difficult issue of recovery of transition costs (discussed infra), is the key to reconciling these competing demands.

Non-discriminatory open access to transmission services is critical to the full development of competitive

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[105]Current Competition, November 1994, Vol. 5, No. 8, at p. 8.

wholesale generation markets and the lower consumer prices achievable through such competition.[106] Transmitting utilities own the transportation system over which bulk power competition occurs and transmission service continues to be a natural monopoly. Denials of access (whether they are blatant or subtle), and the potential for future denials of access, require the Commission to revisit and reform its regulation of transmission in interstate commerce. As discussed in detail in Section IV.B., such action is required by the FPA's mandate that the Commission remedy undue discrimination.

Since the time the NOPR issued, the Commission staff has completed an FEIS that provides a quantitative estimate of some of the cost savings expected from this Rule: approximately $3.8 to $5.4 billion per year. Other non-quantifiable benefits are also expected from this Rule and include: (1) better use of existing assets and institutions; (2) new market mechanisms; (3) technical innovation; and (4) less rate distortion. These potential benefits to the Nation's electricity consumers and the economy as a whole confirm the need to take generic action to remove barriers to competition. In what follows, we set out the changes necessary to remedy undue discrimination and to ensure a fair transition to a more competitive regulatory regime.

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[106]As discussed above, a significant number of public utilities still do not have any form of an "open access" tariff on file with the Commission and no public utility has on file a non-discriminatory open access tariff as defined by this Rule.

IV. Discussion

A. *Scope of the Rule*

1. Introduction

The Commission has determined that non-discriminatory open access transmission services (including access to transmission information) and stranded cost recovery are the most critical components of a successful transition to competitive wholesale electricity markets. These issues are the focal point of this Rule, the accompanying rule on open access same-time information systems, and the accompanying proposed rule on capacity reservation tariffs.

In undertaking these initiatives, however, we are mindful that they are part of a broader picture of evolving issues affecting the electric industry and that other Commission policies will play an important role in ensuring the full development of competitive markets. Among the many issues that are important to competitive bulk power markets are: independent system operators (ISOs); regional transmission groups; generation market power; utility merger policy; and the development of innovative transmission pricing alternatives, such as flow-based, distance-sensitive transmission pricing methodologies that reflect incremental costs. In particular, we believe that ISOs have great potential to assist us and the industry to help provide regional efficiencies, to facilitate economically efficient pricing, and, especially in the context of power pools, to remedy undue discrimination and mitigate market power. Although we discuss some of these issues in this Rule, we will further

develop our policies in other proceedings as well to accommodate and encourage more efficient market structures.

[31,653]

We now address the comments received on the scope of the proposed rulemaking.

2. Functional Unbundling

In the NOPR, the Commission preliminarily found that functional unbundling of wholesale generation and transmission services is necessary to implement non-discriminatory open access transmission.[107] At the same time, the Commission explained that the proposed rule would accommodate, but not require, corporate unbundling (which could include selling generation or transmission assets to a non-affiliate (divestiture) or the less aggressive step of establishing separate corporate affiliates to manage a utility's transmission and generation assets). However, we invited comments on functional unbundling and asked whether it is a strong enough measure to ensure non-discriminatory open access transmission without some form of corporate restructuring.

Comments

Commenters take both sides on whether functional unbundling is sufficient to assure non-discriminatory open access transmission or whether a stronger measure, such as

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[107] *FERC Statutes and Regulations* ¶32,514, at p. 33,080.

corporate unbundling, is needed. Supporting functional unbundling

Various commenters, including utilities and state commissions, generally support functional unbundling as sufficient to assure non-discriminatory open access transmission and oppose requiring corporate unbundling or divestiture.[108] Several commenters state that functional unbundling will remedy discrimination without creating the inefficiencies and additional costs that corporate restructuring would create.[109]

A number of other commenters argue that the Commission has no authority under the FPA to require divestiture of transmission assets.[110] Several of these commenters assert that, even if the Commission has the authority, the electric industry, unlike the natural gas industry, is not ready for mandated corporate unbundling because electric utilities still serve a high percentage of retail customers and own large amounts of the generating capacity.

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[108] *E.g.*, Ohio Edison, UtiliCorp, Pennsylvania P&L, Atlantic City, Montana Power, IL Com, Seattle, OK Com, TX Industrials, MidAmerican, Southwestern, Southern, DOD, Public Service Co of CO, SC Public Service Authority, Florida Power Corp, DOE, WP&L, Com Ed, SBA, Consumers Power, CA Com, UT Com, Houston L&P, KCPL, EEI.

[109] *E.g.*, Florida Power Corp, El Paso, PSNM, and SC Public Service Authority.

[110] *E.g.*, Southwestern, PECO, El Paso, Florida Power Corp, NSP, Public Service E&G, MidAmerican.

They assert that transmission system operation requires the operator to have control over much of the generating capacity.

Various other commenters also support functional unbundling, but believe that safeguards are needed to make it work.[111] Power Marketing Association, for example, suggests a number of safeguards: adoption of cost allocation mechanisms to ensure that utilities do not shift costs from generation to transmission; random audits of utility books; a requirement that each utility file a code of conduct that provides for maximum separation of generation and transmission functions; and active oversight and complaint procedures with strong penalties for abuse. OK Com and GA Com believe that functional unbundling along with the safeguard of the Commission's complaint process will provide sufficient incentive for non-discriminatory open access transmission.

Supporting Corporate Unbundling

A number of commenters see weaknesses in functional unbundling and argue that some form of corporate unbundling is necessary to assure non-discriminatory open access transmission.[112] American Forest & Paper says that there is

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[111]*E.g.*, NRECA, IN Com, Power Marketing Association, TDU Systems, NorAm, Turlock, Texaco, Utility Shareholders, NSP, El Paso, Utility Investors Analysts, PECO, Florida Power Corp, UT Com, Sierra, Carolina P&L, SoCal Gas, OK Com, FL Com, Southern.

[112]*E.g.*, American Forest & Power, American National Power, ND Com, IL Com, UAMPS, NIEP, APPA, Public Power

affiliate abuse in the gas industry and argues that **[31,654]** the electric industry presents even more serious potential for abuse because it is still dominated by vertically integrated utilities.[113] UAMPS asserts that functional unbundling is insufficient because the utility will still favor itself on issues related to transmission planning, capital investment, and operation and maintenance and replacement costs.

NIEP argues that divestiture of generation assets from transmission and distribution is the preferred mechanism for mitigating market power. It further suggests that if corporate divestiture is not feasible the Commission should

Seek to achieve "virtual divestiture" by requiring that the utility generation function be separated from transmission and distribution functions in a separate corporate affiliate, or business unit, and that affiliate transaction rules be established to guard against possible abuses.[114]

It maintains that the Commission has broad authority to protect against undue discrimination and anticompetitive

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Council, Municipal Energy Agency Nebraska, Missouri Basin MPA, Texaco, Direct Services Industries, Calpine, CCEM, Wisconsin Coalition, VT DPS.

[113]*See also* American National Power, ND Com, Calpine.

[114]NIEP Initial Comments at p. 4.

behavior and can order divestiture if such action is required to remedy such behavior.[115]

FTC and DOJ argue that operational unbundling, an example of which is the formation of an independent system operator (ISO), likely would be more effective than functional unbundling and less costly than industry-wide divestiture.[116] FTC describes operational unbundling as "structural institutional arrangements, short of divestiture, that would separate operation of the transmission grid and access to it from economic interests in generation." It gives as an example the California proposal under which utilities would continue to own transmission lines, but an independent system operator would have operational control. DOJ also suggests "a separate authority" to manage the grid and access to the grid, joint ventures, and voluntary pooling arrangements. These commenters argue that operational unbundling would be easier to enforce than functional unbundling.

DOE states that separation of the control of transmission from vertically-integrated companies does not necessarily require a poolco or any particular market mechanism. It suggests the possibility of an ISO that is functionally separate from any buyer or seller of generation, but would not perform all the functions of a poolco.

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[115]*See also* Municipal Energy Agency Nebraska, Direct Services Industries.

[116]Others oppose operational unbundling. *See, e.g.*, Carolina P&L, Salt River.

United Illuminating supports "operational unbundling" that would either (1) eliminate vertical integration and divestiture of transmission assets, leading to the formation of a regional transmission company, or (2) develop a regional contractual approach to transmission services that eliminates the transmission owner's market power and fairly allocates support of the transmission facilities between native load and third-party users of the system. Commission Conclusion

We conclude that functional unbundling of wholesale services is necessary to implement non-discriminatory open access transmission and that corporate unbundling should not now be required. As we explained in the NOPR, functional unbundling means three things:

(1) A public utility must take transmission services (including ancillary services) for all of its new wholesale sales and purchases of energy under the same tariff of general applicability as do others;

(2) A public utility must state separate rates for wholesale generation, transmission, and ancillary services;

(3) A public utility must rely on the same electronic information network that its transmission customers rely on to obtain information about its transmission system when buying or selling power.

We believe that these requirements are necessary to ensure that public utilities provide non-discriminatory

service.[117] These requirements also will give public **[31,655]** utilities an incentive to file fair and efficient rates, terms, and conditions, since they will be subject to those same rates, terms, and conditions.

However, we recognize that additional safeguards are necessary to protect against market power abuses. Functional unbundling will work only if a strong code of conduct (including a requirement to separate employees involved in transmission functions from those involved in wholesale power merchant functions) is in place. In the RINs NOPR, the Commission proposed a code of conduct that would apply to all public utility transmission providers. As the Commission explained,

[T]his code of conduct would require, among other matters, a separation of the utilities' transmission system operations and wholesale marketing functions, and would define permissible and impermissible contacts between employees that conduct wholesale generation marketing functions and employees that handle transmission system operations and reliability in the system control center or at other facilities or locations.[118]

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[117]When and how functional unbundling is to be achieved for requirements transactions and for various types of coordination arrangements, including power pools, is discussed at Sections IV.A.5 and IV.F. Functional unbundling of ancillary services is discussed in Section IV.D.

[118]Real-Time Information Networks and Standards of Conduct, Notice of Proposed Rulemaking, 60 FR 66182 (December 21, 1995), *FERC Statutes and Regulations* ¶32,516 at p. 33,170

Adoption of this code of conduct, discussed in detail in the accompanying final rule on OASIS,[119] is needed to ensure that the transmission owner's wholesale marketing personnel and the transmission customer's marketing personnel have comparable access to information about the transmission system.

As noted by OK Com and GA Com, a further safeguard -- section 206 -- is available if a public utility seeks to circumvent the functional unbundling requirements. Under section 206, any person is free to file a complaint with the Commission detailing any alleged misbehavior on the part of the public utility or its affiliates concerning matters subject to our jurisdiction under the FPA. Similarly, the Commission may, on its own motion, initiate a proceeding to investigate the practices of the public utility and its affiliates.

We believe that functional unbundling, coupled with these safeguards, is a reasonable and workable means of assuring that non-discriminatory open access transmission occurs. In the absence of evidence that functional unbundling will not work, we are not prepared to adopt a more intrusive and potentially more costly mechanism -- corporate unbundling -- at this time.

(1995).

[119]The final rule on information systems no longer uses the terminology RINs. The new terminology used is OASIS -- Open Access Same-time Information System -- which we will use in this Final Rule.

Several commenters discuss the need to encourage or even to require ISOs in the context of functional unbundling. We believe that ISOs have the potential to provide significant benefits (e.g., to help provide regional efficiencies, to facilitate economically efficient pricing, and, especially in the context of power pools, to remedy undue discrimination and mitigate market power) and will further our goal of achieving a workably competitive market. As we learned at our technical conference on power pools, many utilities are examining ISOs and corporate unbundling in various shapes and forms, particularly in the context of power pools. We discuss ISOs extensively in our section on power pools where we believe they will have an important role to play. However, in the context of individual utility transactions, we believe that the less intrusive functional unbundling approach outlined above is all that we must require at this time. Nevertheless, we see many benefits in ISOs, and encourage utilities to consider ISOs as a tool to meet the demands of the competitive marketplace.

As a further precaution against discriminatory behavior, we will continue to monitor electricity markets to ensure that functional unbundling adequately protects transmission customers. At the same time, we will analyze all alternative proposals, including formation of ISOs, and, if it becomes apparent that functional unbundling is inadequate or unworkable in assuring non-discriminatory open access transmission, we will reevaluate our position and decide whether other mechanisms, such as ISOs, should be required.

Finally, while we are not now requiring any form of corporate unbundling, we again encourage utilities to explore whether corporate unbundling or other restructuring **[31,656]**

mechanisms may be appropriate in particular circumstances. Thus, we intend to accommodate other mechanisms that public utilities may submit, including voluntary corporate restructurings (e.g., ISOs, separate corporate divisions, divestiture, poolcos), to ensure that open access transmission occurs on a non-discriminatory basis. We also will continue to monitor -- and stand ready to work with parties engaging in -- innovative restructuring proposals occurring around the country.

3. Market-Based Rates

a. Market-Based Rates for New Generation

In the NOPR, the Commission proposed to codify its determination in Kansas City Power & Light Company[120] that the generation dominance standard for market-based sales from new capacity be dropped.[121] The proposed new section 35.27 would provide:

Notwithstanding any other requirements, any public utility seeking authorization to engage in sales for resale of electric energy at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity first placed in service on or after June 10, 1996.[122]

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[120]67 FERC ¶61,183 at p. 61,557 (1994), *reh'g pending* (KCP&L).

[121]*FERC Statutes and Regulations* ¶32,514 at p. 33,050.

[122]*Id.* at p. 33,154.

However, this proposal would not affect the Commission's continuing authority to look at whether an applicant and its affiliates could erect other barriers to entry and whether there may be affiliate abuse or reciprocal dealing.[123]

Comments

A number of commenters support the Commission's determination in KCP&L[124] and several of them explicitly support the Commission's proposed codification.[125] EEI asserts that more than 50 percent of new generation is from non-utility sources and that recent competitive solicitations for new capacity have been greatly over-subscribed. Entergy argues that there is no evidence in any proceeding thus far of a market power problem in long-run markets.

Other commenters, however, oppose codifying KCP&L.[126] They believe that market power in long-run markets exists for both new and old generation due to, for example, constraints on interface capabilities and unduly long notice periods for replacement of purchases. They argue that

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[123]67 FERC at p. 61,557.

[124]*E.g.*, Entergy, EEI, Atlantic City, Duke Centerior, Houston L&P, Montana-Dakota Utilities, Canadian Petroleum Producers, DOE, Florida Power Corp, PSNM.

[125]*E.g.*, EEI, Centerior, Houston L&P, NYSEG.

[126]*E.g.*, TDU Systems, ELCON, NRECA, Environmental Action, NIEP, APPA, Power Marketing Association, EGA.

there is not enough of a distinction between new and old generation to treat them differently. TDU Systems also notes that the Commission in KCP&L did not take into account the differences between firm and non- firm bulk power. NIEP and ELCON conclude that the Commission erroneously found in KCP&L that no wholesale seller of generation has market power in generation from new facilities. NIEP asserts that in each service area there is usually only one wholesale buyer -- the utility -- who also is virtually always a wholesale seller of generation. Under these circumstances, NIEP argues that there cannot be arm's-length bargaining. Environmental Action complains that the Commission's proposal to codify KCP&L ignores significant factors that impede entry to generation markets, such as utility resistance to purchased power, state government-created barriers to non-utility generation, pancaking of rates under the contract path approach, sunk investment, and scale economies.

Commission Conclusion

In reviewing applications to sell at market-based rates, whether from new (unbuilt) capacity or existing capacity, we require that the seller (and each of its affiliates) must not have, or must have mitigated, market power in generation and transmission and not control other barriers to entry. In order to demonstrate the requisite absence or mitigation of transmission market power, a transmission-owning public utility seeking to sell at market-based rates must have on file **[31,657]** with the Commission an open access transmission tariff for the provision of comparable service. In addition, the

Commission considers whether there is evidence of affiliate abuse or reciprocal dealing.[127]

In KCP&L, we stated that "in light of industry and statutory changes which allow ease of market entry, we therefore will no longer require rate applicants to submit evidence of generation dominance in long-run bulk power markets."[128] We further explained that we had examined "generation dominance in many different cases over the years" and had "yet to find an instance of generation dominance in long-run bulk power markets."[129] Commenters have criticized our findings in KCP&L, but no commenter has provided any evidence of generation dominance in long-run bulk power markets. Moreover, we have seen no such evidence in any of the market-based rate cases we have considered since KCP&L. Based on the comments received, we will codify the Commission's determination in KCP&L that the generation dominance standard for market-based sales from new capacity should be dropped. Because the Commission's findings in KCP&L applied to long-run markets, we will revise proposed §35.27 to apply to sales

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[127]*See, e.g., MidAmerican Energy Company*, 74 FERC ¶61,211 (1996).

[128]*KCP&L*, 67 FERC at p. 61,557. *See also* discussion in proposed rule, *FERC Statutes and Regulations* at pp. 33,067-68.

[129]*Id.*

from capacity for which construction has commenced on or after the effective date of this Rule.[130]

The Commission wishes to clarify that dropping the generation dominance standard for new capacity does not affect the demonstration that an applicant must make in order to qualify for market-based rates for sales from its existing generating capacity. In other words, the fact that an applicant need not demonstrate its lack of generation dominance with respect to new capacity cannot be used to "bootstrap" the authorization of market-based rates for its existing capacity. Moreover, our evaluation of market-based rates for existing capacity will include consideration of new capacity.

In addition, the fact that we are codifying KCP&L does not mean that we will ignore specific evidence presented by an intervenor that a seller requesting market-based rates for sales from new generation nevertheless possesses generation dominance. For example, if the evidence indicated that the new generator, due to its proximity to an existing transmission constraint, could significantly influence the ability to move power across the constraint, we would consider such evidence in determining whether to grant the

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[130]The NOPR's proposed language that a public utility would not have to demonstrate a lack of market power in generation for sales from capacity first placed in service on or after the date 30 days after the final rule is published in the *Federal Register* does not properly reflect the finding in *KCP&L*. Because *KCP&L* addressed new or unbuilt generation, the proposed language is being revised as indicated above and as set forth in the regulatory text included with this Final Rule.

applicant's request.[131] If such evidence is presented, the Commission will evaluate whether the evidence disproves the premise that the seller lacks generation dominance with respect to its new capacity.

If the applicant has existing generation, the sales from which are authorized to be made on a market basis, the Commission would consider whether the new generation (when added to the existing generation with market-based authority) results in the applicant having generation dominance. On the other hand, if the applicant has existing generation, the sales from which are subject to cost-of-service regulation, the Commission would not include this generation in its analysis of the applicant's request for market-based rates for its new generation. The question of whether or not the applicant lacks generation dominance with respect to its existing capacity is relevant only if, and when, the seller applies to the Commission for authority to make wholesale sales for its existing capacity at market-based rates.

If evidence regarding an applicant's generation dominance with respect to its new capacity is submitted, the applicant would be required to provide a satisfactory rebuttal.

[31,658]

b. Market-Based Rates for Existing Generation

In the NOPR, the Commission explained that increased competition resulting from open access transmission may

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[131] *Cf. Wisconsin Electric Power Company, et al.*, 74 FERC ¶61,069 at p. 61,193 (1996).

reduce or even eliminate generation-related market power in the short-run market (sales from existing capacity).[132] Because market power has been the primary concern of the Commission in analyzing requests for market-based rates for such sales, we sought comments on the effect of industry-wide non-discriminatory open access on our criteria for authorizing power sales at market- based rates. The Commission also sought comments on whether the generation dominance standard should be dropped for market-based sales from existing capacity.

Comments

Many commenters support, but many also oppose, market-based rates for existing generation without a case-specific analysis of generation dominance.

Supporting Market-Based Rates for Existing Generation.

Many commenters (primarily IOUs and a number of state commissions) assert that existing generators will not possess market power after implementation of non-discriminatory open access transmission and that market-based rates should be permitted generically for sales from existing generation.[133]

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[132]*FERC Statutes and Regulations* ¶32,514, at pp. 33,093-94.

[133]*E.g.*, EEI, CINergy, Central Illinois Public Service, Citizens Utilities, Com Ed, Ohio Edison, Allegheny, Southern, Portland, NRRI, Pennsylvania P&L, PECO, Dayton P&L, Utilities For Improved Transition, Centerior, Houston L&P, Duke, ConEd,

EEI asserts that market power concerns generally would be transitory, limited to the time needed to build new facilities. Thus, it recommends that all markets be declared competitive by a date certain and that market-based rates then be allowed, with customers permitted to file complaints. Florida Power Corp believes that existing procedures under sections 205 and 206 will adequately protect consumers. Other commenters also urge the Commission to eliminate its generation dominance standard, but assert that the Commission should allow a showing of market dominance in a complaint or show cause proceeding.[134] CT DPUC notes that the Commission should be able to rely on rules of conduct, market mechanisms, and monitoring to curb any market power that may exist.

Utilities For Improved Transition argues that if utilities cannot get market-based rates, the new players in the market will have an unfair advantage, since they do not have to carry the traditional utilities' burden of older, less efficient plants.

Entergy proposes a screening test that would permit the Commission to "deregulate" wholesale sales to certain short-run markets. CINergy recommends that after industry-wide open access tariffs become effective, the Commission adopt a rebuttable presumption that all markets are workably

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IPALCO, Salt River, PJM, NU, NYSEG, Oklahoma G&E, PA Com, OK Com, CT DPUC, CA Com, MT Com.

[134] *E.g.*, Consumers Power, Portland, Dayton P&L, CSW.

competitive; that presumption could be rebutted in a section 206 proceeding.[135]

UtiliCorp, while it believes that market power will probably be fully mitigated by open access, also argues that the Commission should examine generation dominance on a region-by-region basis.[136] Montana-Dakota Utilities argues that the Commission should allow all suppliers in a power pool or RTG to have market-based rates after a Commission finding that there is sufficient generation competition within the region.

Duke states that it would be highly inconsistent for the Commission to require open access, but not allow utilities to compete in the market. It further states that the relevant market should be determined using standard antitrust techniques; the Commission should examine the options available to customers and determine whether the utility possesses monopoly power in a relevant market.

[31,659]

Opposing Market-Based Rates for Existing Generation

Many commenters are concerned that even with open access tariffs certain generators will be able to exercise

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[135] *See also* Citizens Utilities.

[136] *See also* CSW, Industrial Energy Applications, Public Service Co of CO, Coalition for Economic Competition.

market dominance.[137] For example, NARUC argues that utilities retain market power through their ownership of existing generation and transmission facilities, favorable long-term contracts for fuel and other inputs, and access to superior generation sites.[138] NRECA believes that the universe of generation providers is still too narrow to assume a competitive market and that other factors, such as transmission constraints and pancaking of rates, will inhibit the development of competitive markets.[139] FTC says that, although comparable transmission access could broaden the relevant geographic market for generation, the Commission should not assume that there will be no market power. It says that the Commission must continue to evaluate each case.[140]

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[137]*E.g.*, NRECA, TDU Systems, MT Com, SMUD, NEPCO, Orange & Rockland, El Paso, American Forest & Paper, NIPSCO, AEC & SMEPA, OH Com, IL Com, IN Com, Legal Environmental Assistance, LG&E, Cajun, Industrial Energy Applications, LEPA, MA DPU, MI Com, FTC, Minnesota P&L, SC Public Service Authority, WP&L, NARUC, Canadian Petroleum Producers, DOD, CCEM, Environmental Action, American Wind, Cajun, NIEP, EGA, TAPS, ELCON, Consolidated Natural Gas.

[138]*See also* NIEP, Pacificorp, CA Energy Com.

[139]*See also* MT Com, TDU Systems, Soyland.

[140]*See also* AEC & SMEPA, NIPSCO, El Paso (discusses a particular transmission constraint that it states limits its access to suppliers).

NRECA is also concerned that mergers may create a handful of "mega-public utilities" that may affect a regional

TDU Systems argues that the Commission cannot move to market-based rates without a Congressional determination that deregulation of wholesale electric rates should be implemented. It further asserts that the Commission does not have a factual basis for a reasoned conclusion that regulated utilities do not have market dominance -- full open access is only a goal at this time, and the success of open access will depend upon the transmission rate structures the Commission approves.

LEPA raises concerns that the small bulk power suppliers, QFs, co-generators, EWGs, IPPs, and marketers (who provide non- requirements power) may not be able to bring competition to the wholesale market. LEPA concludes that "barriers will exist unless buyers have full access to requirements power itself, rather than just to the chance to acquire the individual components of requirements power."[141] TDU Systems raises concerns about the limited number of generation providers and the effect of possible future mergers. It also argues that pancaked rates raise the cost of transmission to third parties, thereby restricting the geographic scope of markets. As a result, TDU Systems asserts that individual generators in highly concentrated regions will still be able to exert market power. OH Com expresses concerns that restrictions on siting of generation and transmission will favor nearby generators. SC Public Service

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generation market and that the Commission should apply more traditional antitrust principles in analyzing the impacts of mergers.

[141]LEPA Initial Comments Affidavit of William G. Shepherd at p. 4.

Authority argues that if the Commission allows utilities to recover stranded costs their market power will not be mitigated, since customers will have to pay exit fees to switch suppliers.[142]

CCEM notes that in Order No. 636 gas pipelines were not allowed market-based rates for merchant sales until after transmission had been completely unbundled and non-discriminatory open access had been fully implemented.

DOE and DOJ assert that open access should not be assumed to mitigate market power sufficiently to justify deregulation of existing generation -- structural changes, such as control of the regional grid by an independent entity, are required. DOE requests that the Commission continue to look for affiliate abuse when reviewing market-based rates for new generation. Similarly, EPA is concerned that even with open access, individual generators may still exert market power by their domination of a particular geographic market. It is also concerned **[31,660]** that low-cost plants that are subject to weaker environmental standards could have a market advantage. NEPOOL Review Committee requests that the Commission not approve any market prices "where the market into which the seller proposes to sell is not effectively competitive due to the absence of regional transmission products and prices."[143]

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[142]*See also* DOD and WP&L. IL Com suggests that the Commission allow market-based rates to a utility on the condition that the utility forego stranded cost recovery.

[143]NEPOOL Review Committee Initial Comments at p. 28.

Commission Conclusion

While the Commission expects this Rule to facilitate the development of competitive bulk power markets, we find that there is not enough evidence on the record to make a generic determination about whether market power may exist for sales from existing generation. We continue to have concerns about how to define the relevant markets and believe that a more rigorous analysis is needed than can be achieved with the limited market data that is now available. We will continue our case-by-case approach that allows market-based rates based on an analysis of generation market power in first tier and second tier markets.[144] In particular cases, however, the effect of the mandatory open access prescribed by this Final Rule may lead to the consideration of geographic markets for the applicant's generation products that are broader in scope than the first-tier and second-tier markets currently considered.[145] By the same token, in some cases,

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[144]*See, e.g., Southwestern Public Service Company*, 72 FERC ¶61,208 at p. 61,996 (1995).

[145]The Commission's practice is to define the relevant markets as those utilities directly interconnected to the applicant (first-tier markets). For each first-tier market, we consider all utilities interconnected to the first-tier utility and all utilities interconnected to the applicant as competitors in that relevant market. Thus, the competitors include the second-tier utilities directly interconnected to the relevant market and those other first-tier utilities that can reach the market by virtue of the applicant's open access transmission tariff. *See, e.g., Kansas City Power & Light Company*, 67 FERC ¶61,183 at p. 61,556; and *Heartland Energy Services, Inc.*, 68 FERC ¶61,223 at p. 62,061.

evidence of the effects of transmission constraints may circumscribe the scope of the relevant geographic market for the applicant's generation products.

While we will continue to apply the first-tier/second-tier analysis, we will allow applicants and intervenors to challenge the presumption implicit in the Commission's practice that the relevant geographic market is bounded by the second-tier utilities. Thus, for instance, applicants may present evidence that the relevant market is in fact broader than the first or second tier. In support of such a contention, an applicant would need to show more than the existence of open access. For example, an applicant might attempt to demonstrate the lack of significant transmission constraints in the more broadly defined market and that cumulative transmission rates would not significantly affect the ability of more distant suppliers to compete in the relevant market. Similarly, an intervenor may present evidence that, due to the existence of significant transmission constraints within the first- and second-tier markets, the relevant market is in fact more limited in scope.[146]

Finally, we will maintain our current practice of allowing market-based rates for existing generation to go into effect subject to refund. To the extent that either the applicant or intervenors in individual cases offer specific evidence that the relevant geographic market ought to be defined differently than under the existing test, we will examine such arguments through formal or paper hearings.

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[146]*See Wisconsin Public Service Corporation*, 75 FERC ¶61, --, slip op. at pp. 6-7 (1996).

Because our goal is to develop more competitive bulk power markets, we will continue to monitor markets to assess the competitiveness of the market in existing generation, and we will modify our market rate criteria if and when appropriate. However, any changes we might make to our analysis for authorizing market-based rates in the future will not upset transactions entered into pursuant to existing market-based rate authority. The policies we put in place today to develop a smoothly functioning transmission access regime will provide useful experience and information for assessing the effects of generation concentration.

4. Merger Policy

In the NOPR, the Commission did not address possible ramifications of the **[31,661]** NOPR with regard to its existing merger policy.

Comments

A number of commenters suggest that the Commission should reevaluate its merger policy in light of the NOPR.[147] They further suggest a number of changes that they believe need to be made to the Commission's existing merger policy.

Most commenters raising this issue express concerns that mergers will lessen competition and hinder achievement of competitive bulk power markets.[148] For example, NRECA

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[147] *E.g.*, NRECA, TAPS, Wisconsin Coalition, APPA.

[148] *E.g.*, Wisconsin, Rosebud, NRECA, IN Com, Wisconsin Coalition, NIEP, Minnesota P&L, APPA.

indicates that the Commission's merger policy is at a crossroads. It believes that it is essential for the Commission to reevaluate its merger policy in concert with the proposed rulemakings.[149] Similarly, TAPS recommends that the Commission reevaluate its merger criteria to ensure that in a more competitive era, mergers are found to be consistent with the public interest only if they are pro-competitive. Several commenters argue that the Commission should continue to conduct a case-by-case investigation of the product and geographic markets that will be affected by a proposed merger.[150]

A number of commenters also suggest certain changes that they would like to see in the Commission's merger policy.[151] APPA recommends that, at a minimum, all merger approvals considered by the Commission should be conditioned on: (1) filing an open access transmission tariff, (2) demonstrating no market power in generation or ancillary services, and (3) granting all existing requirements customers of the merged entity the right to convert existing contracts to rights to equivalent transmission capacity. Several commenters suggest adopting the U.S. Department of Justice Merger Guidelines in analyzing merger proposals.[152]

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[149]*See also* APPA.

[150]*E.g.*, Wisconsin Coalition, MMWEC.

[151]*E.g.*, APPA, Wisconsin Coalition, Minnesota P&L, IN Com.

[152]*E.g.*, Wisconsin Coalition.

Environmental Action and others contend that merging utilities must be required to demonstrate real net benefits to retail and wholesale customers that could not otherwise be achieved but for the proposed merger.[153]

Commenters also argue that the Commission should use its merger conditioning authority to order divestiture of transmission and generation when required to ensure competition.[154] Environmental Action and NEPOOL Review Committee suggest conditioning merger applications on the existence of regional transmission pricing arrangements to mitigate any generation market power gained by the merging entities.

Commission Conclusion

The Commission appreciates the concerns and suggestions raised with respect to our merger policy. However, since the time the NOPR was issued (and comments received thereon), we issued a Notice of Inquiry on the Commission's merger policy in Docket No. RM96-6-000.[155] There we indicated that we will review whether our criteria and policies for evaluating mergers need to be modified in light of the changing circumstances, including this final rule, that are occurring in the electric industry. The NOI proceeding will permit us to consider comments from all

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[153]E.g., TAPS, Wisconsin Coalition.

[154]*E.g.*, NIEP, Wisconsin Coalition, TAPS, Environmental Action.

[155]*FERC Statutes and Regulations* ¶35,531 (1996).

interested participants and, at the same time, allow us to review our merger criteria and policies in light of this final rule. We are committed to reviewing our merger policy in a timely manner in the ongoing NOI proceeding.[156]

5. Contract Reform

In the NOPR, the Commission explained that it believed that it could remedy unduly discriminatory practices and achieve more competitive bulk power markets without abrogating existing **[31,662]** wholesale power supply contracts that bundle generation and transmission services and existing wholesale transmission contracts.[157] Thus, we proposed to apply the functional unbundling requirement only to transmission services under new requirements contracts, new coordination contracts, and new transactions under existing coordination contracts. However, the Commission did invite comment on whether it would be contrary to the public interest to allow all or some of the above types of existing contracts to remain in effect.

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[156]Our decision to review our merger policy in a separate NOI proceeding is not intended to affect a utility's business decision of whether a merger may be in the economic interest of its ratepayers and stockholders. The NOI proceeding will not prevent us from reviewing merger applications in as timely a manner as possible.

[157]*FERC Statutes and Regulations* ¶32,514 at p. 33,093.

Requirements and Transmission Contracts

Many of the commenters (including utility customers and third-party power suppliers) addressing this issue oppose abrogating existing contracts on a generic basis.[158] A number of the commenters contend that existing contracts should be retained because they are the result of mutually beneficial bargaining.[159] SMUD and TANC are concerned that existing contracts providing for transmission service that is superior to the pro forma tariffs not be abrogated.[160] Ohio Edison argues that existing contracts have contributed to the emergence of competition, meet the specific needs of the parties, have been approved by the Commission, and have not been found to be unduly discriminatory or violative of the public interest, and that their preservation is consistent with the Energy Policy Act, most notably amended section 211 of the FPA. PacifiCorp and AEP express concern that contract abrogation

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[158]*E.g.*, Dayton P&L, NSP, Montaup, Southwestern, Ohio Edison, Consumers Power, Allegheny, Public Generating Pool, NEPCO, Pennsylvania P&L, Southwest TDU Group, Arizona, DOD, El Paso, Florida Power Corp, AEC & SMEPA, Atlantic City, Texaco, Tampa, CSW, Central Illinois Public Service, CA Cogen, ConEd, GA Com, Consolidated Natural Gas, Ohio Valley, Pacific Northwest Coop, Salt River, Oglethorpe, Minnesota P&L, NYSEG, Brazos, Southern, Washington Water Power, CINergy, SoCal Edison, Hoosier EC.

[159]*E.g.*, AEC & SMEPA, Cajun, Carolina P&L, NSP, Pennsylvania P&L, UNITIL, Southwestern, CSW.

[160]*See also* Dairyland, DE Muni, Arkansas Cities, Ohio Valley.

would create competitive instability. American Forest & Paper argues that the Commission cannot refuse to honor existing contracts if it expects a competitive bulk power market to emerge.

Numerous commenters further argue that contract abrogation requires a fact-based, contract-specific evaluation, and they oppose any generic declaration that existing contracts are contrary to the public interest.[161] Some suggest that generic contract abrogation cannot be justified under the public interest standard.[162]

Missouri Basin MPA argues that the Commission should allow abrogation of existing wholesale power and transmission arrangements if the customer can demonstrate the undue competitive disadvantage caused by the arrangement.

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[161] *E.g.*, AEP, Associated EC, DOD, El Paso, NEPCO, Ohio Edison, PSNM, Southwest TDU Group, Utilities For Improved Transition, NYSEG, Citizens Utilities, NM Com, EGA. See also NRECA, TDU Systems, Blue Ridge, CCEM, Industrial Energy Applications, APPA, Cajun, Springfield, DE Muni, Missouri Basin MPA, TANC, Wolverine Coop Members, FL Com, Citizens Utilities, Soyland (support contract abrogation on a case- by-case basis).

[162] *E.g.*, Utilities For Improved Transition, NSP, Southwestern, DE Muni.

A few commenters support some form of generic contract abrogation.[163] CCEM asserts that existing wholesale requirements customers must be given the right to convert to transmission service under non-discriminatory open access tariffs.[164] CCEM notes that this is the same relief from undue discrimination that the Commission afforded to pipeline customers in Order Nos. 436 and 500.[165] CCEM emphasizes that here, in contrast to what occurred in the gas industry, "[c]onversion rights should be understood as the logical quid pro quo for introducing extra-contractual stranded-cost recovery rights into the wholesale requirements **[31,663]** contracts of electric utilities."[166] NRECA asserts that it would be unduly discriminatory to allow new transmission customers to use the open access transmission tariffs, but not allow existing customers the same access.[167]

TAPS says that if those who now have discriminatory contracts are forced to live with those contracts, a fully

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[163]*E.g.*, NRECA, CCEM, ELCON, DE Muni, Oglethorpe. Portland maintains that it would be in the public interest to abrogate existing contracts completely, but recommends that such action be taken only on a case-by-case basis.

[164]*See also* VT DPS, NYMEX.

[165]*See also* VT DPS, Portland.

[166]CCEM Initial Comments at p. 26. *See also* ELCON, VT DPS, Blue Ridge, NYMEX, OK Com, Missouri Basin MPA, Texas-New Mexico, TDU Systems.

[167]*See also* TDU Systems, Texas-New Mexico, TAPS, Wisconsin Municipals.

competitive market will be delayed considerably.[168] Moreover, TAPS argues, the Commission has a statutory duty to remedy the undue discrimination that it is only now recognizing. Even if the Commission will not abrogate these contracts across the board, TAPS asserts that we should use our section 206 authority to do so on a contract-by-contract basis.

San Francisco requests that the Commission clarify that a holder of capacity rights under an existing contract can extend contractual rights to transmission access at least coterminous with the life of the project and under a roll-over or renewal contract on the same basis as provided in the existing contract. Anoka EC proposes that when a wholesale purchaser's contract expires, it should have a right of first refusal to contract for the transmission capacity to which it previously had a right. Knoxville urges the Commission to require renegotiation of the notice and/or term of all existing contracts for which the voluntary termination period exceeds the time frame for implementation of the final rule.

NEPCO suggests that we require existing power contracts that allow rate changes to be separated into their generation and transmission components, without otherwise disturbing their terms; this would allow comparisons between

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[168] *See also* NorAm. UtiliCorp argues that existing contracts should not be allowed to extend indefinitely (as through "evergreen" clauses) without adopting comparability. *See also* Texaco, Wisconsin Municipals, Phelps Dodge.

the transmission service the utility provides to its power customers and the service it offers to others.[169]

Coordination Agreements

CINergy argues that coordination agreements should not be excluded from the comparability standard and that the Commission should use its authority under section 206 to require amendments to such agreements, just as it did in Order 636 in requiring unbundling of pipeline supply contracts. CINergy suggests that public utilities should be given up to three years to file the amendments to avoid hardship on the industry and the Commission's staff. CINergy further asserts that future transactions conducted under coordination agreements should be unbundled and the transmission component subjected to the comparable transmission service requirement.

Others argue that purchases under existing coordination agreements made on behalf of retail native load should not be unbundled.[170] NY Com and IL Com recommend that proposed §35.28(c) be modified to state that the functional unbundling requirement "exclude(s) those wholesale purchases made by the utility to serve existing or expected native retail load."

Utilities For Improved Transition disagrees with the idea that new transactions under existing coordination

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[169]*See also* Industrial Energy Applications.

[170]*E.g.*, Con Ed, Detroit Edison, IL Com.

agreements should be subject to the rule.[171] It argues that the sanctity of coordination contracts should be the same as for other contracts. Coordination contracts are not simply agreements to agree in the future, according to Utilities For Improved Transition; they set forth terms and rates and merely leave the timing of transactions to be resolved in the future. Moreover, it argues that the Commission has given no reason to abandon its practice of encouraging coordination sales by allowing price flexibility.

Commission Conclusion

Requirements and Transmission Contracts

We do not believe it is appropriate to order generic abrogation of existing requirements and transmission contracts. While the Commission did generically **[31,664]** find it appropriate to modify natural gas contracts to complete the move to a competitive commodity market in natural gas, we face a different situation here. At the time the Commission addressed this situation in the natural gas industry, it was faced with shrinking natural gas markets, statutory escalations in natural gas ceiling prices under the Natural Gas Policy Act, and increased production of gas.[172] In other words, there was a market failure in the industry that required the extraordinary measure of generically allowing all customers to break their contracts with pipelines.

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[171] *See also* Utility Workers Union, VEPCO.

[172] *See* Pierce, Richard J., *Reconstituting the Natural Gas Industry from Wellhead to Burnertip*, 9 Energy L.J. 1 (1988).

In contrast, there is no such market failure in the electric industry. Although changes in the industry have been and continue to be dramatic, we do not believe they compel generic abrogation of requirements and transmission contracts.[173]

While we have concluded that current conditions in the wholesale power market do not warrant the generic modification of requirements contracts, we conclude nonetheless that the modification of certain requirements contracts on a case-by-case basis may be appropriate. We conclude further that, even if customers under such contracts are bound by so-called Mobile-Sierra clauses, they nonetheless ought to have the opportunity to demonstrate that their contracts no longer are just and reasonable.

The Commission finds that it would be against the public interest to permit a Mobile-Sierra clause in an existing wholesale requirements contract to preclude the parties to such a contract from the opportunity to realize the benefits of the competitive wholesale power markets. For purposes of this finding, the Commission defines existing requirements contracts as contracts executed on or before July 11, 1994.[174]

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[173]In addition, we do not believe that unfavorable requirements contracts will derail the attainment of competitive wholesale power markets. Indeed, many of the commenters support this position and seek to retain their existing requirements contracts.

[174]This is consistent with the definition of existing requirements contracts we have used for purposes of stranded cost recovery.

By operation of this finding, a party to a requirements contract containing a Mobile-Sierra clause no longer will have the burden of establishing independently that it is in the public interest to permit the modification of such contract. The party, however, still will have the burden of establishing that such contract no longer is just and reasonable and therefore ought to be modified.

This finding complements the Commission's finding that, notwithstanding a Mobile-Sierra clause in an existing requirements contract, it is in the public interest to permit amendments to add stranded cost provisions to such contracts if the public utility proposing the amendment can meet the evidentiary requirements of this Rule.[175] The Commission's complementary Mobile-Sierra findings are not mutually exclusive. Any contract modification approved under this Section shall provide for the utility's recovery of any costs stranded consistent with the contract modification. The stranded costs must be prudently incurred, legitimate and verifiable, as provided in Section IV.J. Further, the Commission has concluded that if a customer is permitted to argue for modification of existing contracts that are less favorable to it than other generation alternatives, then the utility should be able to seek modification of contracts that may be beneficial to the customer.

The Commission believes that the most productive way to analyze contract modification issues is to consider simultaneously both the selling public utility's claims, if any, that it had a reasonable expectation of continuing to serve the

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[175] *See* Section IV.J.5.

customer beyond the term of the contract and the customer's claim, if any, that the contract no longer is just and reasonable and therefore ought to be modified. Thus, if the selling public utility intends to claim stranded costs, it must present that claim in any section 206 proceeding brought by the customer to shorten or terminate the contract. Similarly, if the customer intends to claim that the notice or termination provision of its existing requirements contract is unjust and unreasonable, it must present that claim in any proceeding brought by the selling public utility to seek recovery of stranded costs. This will promote administrative **[31,665]** efficiency and will permit the Commission to consider how the contracting parties' claims bear on one another.

The Commission does not take contract modification lightly. Whether a utility is seeking a contract amendment to permit stranded cost recovery based on expectations beyond the stated term of the contract, or a customer is seeking to shorten or eliminate the term of an existing contract, we believe that each has a heavy burden in demonstrating that the contract ought to be modified. Still, we believe that given the industry circumstances now facing us, both selling utilities and their customers ought to have an opportunity to make the case that their existing requirements contracts ought to be modified. By providing both buyers and sellers this opportunity, the Commission attempts to strike a reasonable balance of the interests of all market participants. The Commission expects that many of the arguments presented by buyers and sellers in such proceedings will be fact specific.

We note that because we are not abrogating existing requirements and transmission contracts generically and because the functional unbundling requirement of the Final

Rule applies only to new wholesale services, the terms and conditions of the Final Rule pro forma tariff do not apply to service under existing requirements contracts. However, if a customer's existing bundled service (transmission and generation) contract or transmission-only contract expires, and the customer takes any new transmission service from its former supplier, the terms and conditions of the Final Rule tariff would then apply to the transmission service that the customer receives.

A further issue concerning firm contract customers is their right to transmission capacity (and the rate for such capacity) when their contracts expire by their own terms or become subject to renewal or rollover. We have concluded that all firm transmission customers (requirements and transmission-only), upon the expiration of their contracts or at the time their contracts become subject to renewal or rollover, should have the right to continue to take transmission service from their existing transmission provider. The limitations are that the underlying contract must have been for a term of one-year or more and the existing customer must agree to match the rate offered by another potential customer, up to the transmission provider's maximum filed transmission rate at that time, and to accept a contract term at least as long as that offered by the potential customer.[176] This means that there is no right to grandfather

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[176]This right of first refusal exists whether or not the customer buys power from the historical utility supplier or another power supplier. If the customer chooses a new power supplier and this substantially changes the location or direction of its power flows, the customer's right to continue taking transmission service from its existing transmission provider may be affected by

the historical price of the transmission service. Thus, if not enough capacity is available to meet all requests for service, the right of first refusal gives the capacity to the existing customer who had contractually been using the capacity on a long-term, firm basis, assuming that it meets the conditions set forth above. Moreover, this limited right of first refusal is not a one-time right of first refusal for contracts existing as of the date of the final rule, but is an ongoing right that may be exercised at the end of all firm contract (including all future unbundled transmission contracts) terms. A customer converting existing bundled service to the Final Rule pro forma tariff would not have a reservation priority for capacity expansions, unless the existing contract provides for future transmission to the customer that requires capacity expansion.[177]

Finally, with respect to all existing requirements contracts and tariffs that provide for bundled rates, we will require all public utilities to make informational filings setting forth the unbundled power and transmission rates reflected in those contracts and tariffs. These informational rates must be submitted to the Commission within 60 days of publication of the Final Rule in the Federal Register and must also be included as a line item on all bills submitted to wholesale customers in the third month following the effective date of this final rule. The unbundled **[31,666]** informational rates will permit wholesale customers to compare rates in

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transmission constraints associated with the change.

[177]The above discussion on a right of first refusal addresses firm contract customers. However, the same logic applies to retail customers.

anticipation of their contracts expiring so that they can evaluate alternative contracts. Coordination Agreements

The situation as to coordination agreements requires a slightly different approach.[178] While we also believe that as a general matter it is important not to generically abrogate any coordination agreements, this is particularly true for non-economy energy coordination agreements that may reflect complementary long-term obligations among the parties. This type of agreement presents special problems and, as discussed below, we will not generically require this type of coordination agreement to be modified.[179]

Hundreds of coordination agreements exist in the industry today. Many are open-ended agreements that permit new transactions to occur well into the future. Because these contracts may not expire of their own terms in a reasonable

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[178]For purposes of this discussion, we define coordination agreements as all power sales agreements, except requirements service agreements. In addition, for purposes of implementing the non-discriminatory, open access requirements of the Final Rule, we are dividing bilateral coordination agreements into two general categories: (1) *Economy energy coordination agreements* are contracts and service schedules thereunder that provide for trading of electric energy on an "if, as, and when available" basis, but do not require either the seller or buyer to engage in a particular transaction; and (2) *non-economy energy coordination agreements* are any non-requirements service agreements, except economy energy coordination agreements.

[179]The requirements for power pools and other multilateral arrangements are discussed in detail in Section IV.F.

time, they may present a larger and more enduring obstacle to non-discriminatory open access and more competitive bulk power markets. Thus, to assure that non-discriminatory open access becomes a reality in the relatively near future, we will partially modify existing economy energy coordination agreements. We will condition future sales and purchase transactions under existing economy energy coordination agreements[180] to require that the transmission service associated with those transactions be provided pursuant to this Rule's requirements of non-discriminatory open access, no later than December 31, 1996.[181] We also will require that for new economy energy coordination agreements[182] where the transmission owner uses its transmission system to make economy energy sales or purchases, the transmission owner must take such service under its own transmission tariff as of the date trading begins under the agreement.[183]

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[180]Those executed prior to 60 days after publication of the Open Access Rule in the *Federal Register*.

[181]The requirement to unbundle future transactions under existing economy energy coordination agreements means that if the transmission owner uses its transmission system to make economy energy coordination sales or purchases, it must take service for these transactions under its own transmission tariff after December 31, 1996.

[182]Those executed 60 days after publication of the Open Access Rule in the *Federal Register*.

[183]Accordingly, transmission service needed for sales or purchases under *all* new economy energy coordination agreements will be pursuant to the Final Rule pro forma tariff.

Finally, we will treat non-economy energy coordination agreements differently. We will not require their modification. However, this does not insulate such agreements from complaints that transmission service provided under such agreements be provided pursuant to the Final Rule pro forma tariff.

With respect to coordination pricing practices, we conclude that non-discriminatory open access consistent with the requirements of this Rule is necessary if we are to allow utilities to continue to use market-driven pricing, such as split-the-savings pricing, for coordination sales. Absent such non-discriminatory open access, a utility would be able to deny access to others so as to obtain a higher price for its own power sales.

6. Flow-Based Contracting and Pricing

In the NOPR, the Commission discussed the procedures to be used in establishing Stage One rates. These Stage One rates were proposed as an administrative convenience. The proposal merely followed the long-established practice of establishing rates on the basis of contract **[31,667]** path pricing.[184] The Commission made no

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[184]A contract path is simply a path that can be designated to form a single continuous electrical path between the parties to an agreement. Because of the laws of physics, it is unlikely that the actual power flow will follow that contract path.

determination with respect to the appropriateness of flow-based pricing or contracting for other purposes.[185]

Most of the commenters addressing this issue recommend that industry or the Commission -- either in this rule or ultimately -- dispense with the traditional contract path basis for pricing and contracting. Most commenters also recommend that the Commission adopt or encourage a regional approach to the solution of transmission pricing problems, though they differ markedly in how to account for flows.[186]

Transmission customers generally seek to rid themselves of "pancaked" transmission rates that are associated with the traditional approach to transmission pricing.[187] They propose the development of regionwide transmission rates, perhaps determined on a pool or RTG

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[185]Flow-based pricing or contracting would be designed to account for the actual power flows on a transmission system. It would take into account the "unscheduled flows" that occur under a contract path regime. .

[186]*E.g.*, APPA, TAPS, NY Energy Buyers, Arcadia, Brownsville, Detroit Edison Customers, AMP-Ohio, Michigan Systems.

[187]*E.g.*, AMP-Ohio, NRECA, APPA, Detroit Edison Wholesale Customers, MMWEC, Missouri Basin MPA, Air Liquide, American Wind Energy, Associated Power, CCEM.

basis. Most, however, do not discuss how to account for unscheduled flows.[188]

Many transmission providers, some regulatory authorities, and some individuals strongly support flow-based pricing. Most of these commenters recognize a need for a regional approach to resolve transmission pricing concerns.[189] However, many of them also appear to accept contract pricing in the near term because of the need to implement open access quickly. [190]NERC recommends that the Commission maintain an open position on the transfer scheduling process and supports changes in the process to reflect actual power flows. EEI suggests that the Commission should be willing to deviate from a contract path approach, since competition may be accompanied by greater unscheduled flows and contract pricing is not well equipped to deal with such flows.

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[188]Some commenters propose the development of a regional rate on a postage stamp basis, without regard to distance travelled or the actual path of power flows. *E.g.*, Air Liquide, American National Power, CA Energy Co. Several commenters do, however, propose ways to account for unscheduled flows. *E.g.*, American Forest & Paper, DE Muni, Lower Colorado River Authority.

[189]*E.g.*, CSW, EDS Utilities, Dominion, CINergy, KS Com, CT DPUC, Com Ed, Hogan.

[190]NYMEX favors contract path pricing because of its familiarity and believes that the issue should primarily be resolved by the transmitting utilities. AEP believes that the primary responsibility lies with industry to develop alternative pricing structures.

However, EEI concludes that a single approach to pricing will not be appropriate for all systems.

Other commenters, however, do raise concerns with respect to flow-based pricing. AEC & SMEPA considers flow-based pricing to be flawed because that method makes an individual customer responsible for load flow effects caused by a third party's development of the third-party's transmission system over which the customer and its transmission provider had no control. Dayton P&L fears that competition would be lessened under flow- based pricing because utilities with large transmission systems would dominate the market.

Several commenters oppose Southern's and United Illuminating's flow-based proposals, arguing that the methodologies are based on estimates of actual flows or a set of conditions with limited applicability. Various commenters also believe that a single rate is flawed and could cause just as many problems as contract path pricing.[191]

Most commenters appear to believe that the Commission endorsed contract path pricing in the NOPR. Hogan expresses concern that many industry participants' understanding of the pro forma tariffs is based on the fiction of the contract path. The MT Dept of Environmental **[31,668]** Quality believes that despite the Commission's pledge to consider innovative pricing proposals,[192] such proposals will

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[191] *E.g.*, NU, NEPCO, BECO, Florida Power Corp.

[192] *See FERC Statutes and Regulations* ¶31,005.

receive heavy scrutiny, while conventional contract path pricing proposals will receive nearly automatic approval. Dominion is concerned that relying on the initiative of individual transmission owners to develop flow- based pricing will yield slow and patchy results.

Commission Conclusion

We will not, at this time, require that flow-based pricing and contracting be used in the electric industry. In reaching this conclusion, we recognize that there may be difficulties in using a traditional contract path approach in a non- discriminatory open access transmission environment, as described by Hogan and others. At the same time, however, contract path pricing and contracting is the longstanding approach used in the electric industry and it is the approach familiar to all participants in the industry. To require now a dramatic overhaul of the traditional approach -- such as a shift to some form of flow-based pricing and contracting -- could severely slow, if not derail for some time, the move to open access and more competitive wholesale bulk power markets. In addition, we believe it is premature for the Commission to impose generically a new pricing regime without the benefit of any experience with such pricing. We welcome new and innovative proposals, but we will not impose them in this Rule.

While we are not requiring the use of any form of flow-based pricing, we recognize that some versions of flow-based pricing could have benefits. For example, some versions of flow-based pricing could more accurately reflect and price the actual power flows on transmission systems and thus could produce efficiency gains, better generation siting

decisions, and benefits for customers and utilities alike. Other versions could more accurately assign capacity rights in accordance with a party's contribution to capacity costs.

These potential benefits, however, will not simply come about in the abstract. Flow-based pricing methodologies that will achieve the benefits sought by most of the participants in the industry are in a development stage and require further work and refinement to address some of the difficulties associated with flow-based approaches. Concurrent work on OASIS and resolving available transmission capability issues may help resolve flow-based issues. However, as demonstrated by the paucity of possible methodologies presented in the comments, developing workable methodologies will be difficult. As we explained in our Transmission Pricing Policy Statement, we are receptive to proposals for alternative rate methodologies, such as distance-sensitive and flow-based pricing, as long as the proposals are well supported. However, we have yet to receive a formal rate application for a flow-based pricing methodology that has been tested enough that it can be required on a generic basis. Thus, we have decided to go forward to achieve open access and more competitive wholesale bulk power markets without waiting for the development of a generic flow-based pricing methodology.

We wish to emphasize further that in taking this approach we are not endorsing the traditional contract path approach as the only available approach. We continue to approve contract path pricing because it is the long-established pricing method that comes to us in rate filings by the electric industry, is administratively convenient and feasible, and thus is a practical way to move forward now. We remain open to

alternative methodologies, but need to see better developed approaches from the industry before we can consider generic adoption of alternative pricing.

We also believe the adoption of flow-based pricing will be more practical on a regional, instead of individual utility, basis. Some forms of flow-based pricing may even require a regional approach. To this extent, regional ISOs could be a valuable mechanism for implementing such pricing reforms.

B. *Legal Authority*

The Commission reaffirms its conclusion in the NOPR that we have the authority under the FPA to order wholesale transmission services in interstate commerce to remedy undue discrimination by public utilities. We analyze below the relevant cases examining our wheeling authority, **[31,669]** then discuss and respond to the legal arguments raised by the commenters.

1. Bases for Legal Authority

a. Undue Discrimination/Anticompetitive Effects

In upholding the Commission's order requiring non-discriminatory open access in the natural gas industry, the court in Associated Gas Distributors v. FERC stated that the Natural Gas Act "fairly bristles" with concern for undue

discrimination.[193] The same is true of the FPA. The Commission has a mandate under sections 205 and 206 of the FPA to ensure that, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, no person is subject to any undue prejudice or disadvantage. We must determine whether any rule, regulation, practice or contract affecting rates for such transmission or sale for resale is unduly discriminatory or preferential, and must prevent those contracts and practices that do not meet this standard. As discussed below, AGD demonstrates that our remedial power is very broad and includes the ability to order industry- wide non-discriminatory open access[194] as a remedy for undue discrimination. The AGD court reached this decision even in the face of prior cases that acknowledged that Congress did not mandate common carriage or explicitly empower the Commission to order direct access for either gas transporters or electric utilities. Moreover, the Commission's power under the FPA "clearly carries with it the responsibility to consider, in appropriate circumstances, the anticompetitive effects of regulated aspects of interstate utility operations pursuant to

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[193]*Associated Gas Distributors v. FERC*, 824 F.2d 981, 998 (D.C.Cir. 1987), *cert. denied*, 485 U.S. 1006 (1988) (AGD).

[194]We use the term "open access" to refer to a public utility's obligation to put a tariff on file offering service to eligible customers. Access is not open to all. Specifically, the tariff is not an offer to serve retail customers if state law does not permit retail wheeling.

(FPA) sections 202 and 203, and under like directives contained in sections 205, 206, and 207."[195]

Therefore, based on the mandates of sections 205 and 206 of the FPA and the case law interpreting the Commission's authority over transmission in interstate commerce, we conclude that we have ample legal authority -- indeed, a responsibility -- under section 206 of the FPA to order the filing of non-discriminatory open access transmission tariffs if we find such order necessary as a remedy for undue discrimination or anticompetitive effects.[196] We discuss below the primary court decisions that touch on our wheeling authority under sections 205 and 206.

The Commission's authority to order access as a remedy for undue discrimination under the Natural Gas Act (NGA) was upheld and discussed in detail in AGD. In AGD, the court upheld in relevant part the Commission's Order No.

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[195]*Gulf States Utilities Company v. FPC*, 411 U.S. 747, 758-59 (1973).

[196]In most situations, discrimination that precludes transmission access or gives inferior access will have at least potential anticompetitive effects because it limits access to generation markets and thereby limits competition in generation. Similarly, it is probable that any transmission provision that has anticompetitive effects would also be found to be unduly discriminatory or preferential because the anticompetitive provision would most likely favor the transmission owner vis-a-vis others.

436.[197] That order found the prevailing natural gas company practices to be "unduly discriminatory" within the meaning of section 5 of the NGA (the parallel to section 206 of the FPA) and held that if pipelines wanted blanket certification for their transportation services, they must commit to transport gas for others on a non-discriminatory basis; in other words, they must provide non-discriminatory open access.

In upholding the Commission's authority to require open access, the court first noted that the opponents' arguments against such authority must proceed "uphill." The statute contains no language forbidding the Commission to impose common carrier status on pipelines, let alone forbidding the Commission to impose "a specific duty that happens to be a typical or even core component of such status." The court found that the legislative **[31,670]** history cited by the opponents came nowhere near overcoming this statutory silence. Rather, the legislative history supported only the proposition that Congress itself declined to impose common carrier status.[198] Emphasizing Congress' deep concern with undue discrimination, the court found that the Commission had ample authority to "stamp out" such discrimination:

The issue seems to come down to this: Although Congress explicitly gave the Commission the power and the duty to achieve one of the prime goals of common carriage

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[197]Order No. 436, Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol, *FERC Statutes and Regulations* ¶30,665 (1985).

[198]*AGD*, *supra*, 824 F.2d at p. 997.

regulation (the eradication of undue discrimination), the Commission's attempted exercise of that power is invalid because Congress in 1906 and 1914 and 1935 and 1938 itself refrained from affixing common carrier status directly onto the pipelines and from authorizing the Commission to do so. And this proposition is said to control no matter how sound the Order may be as a response to the facts before the Commission. We think this turns statutory construction upside down, letting the failure to grant a general power prevail over the affirmative grant of a specific one.[199]

The AGD court found that court decisions under the FPA did not support the view that the Commission's authority to "stamp out" undue discrimination is hamstrung by an inability to require non-discriminatory open access as a remedy. These decisions are discussed below.

One of the earliest cases on wheeling is Otter Tail Power Company v. United States (Otter Tail).[200] In that case, the Supreme Court rejected the argument that the District Court, in a civil antitrust suit, could not order wheeling because to do so would conflict with the FPC's purported wheeling authority.[201] The Court explained that Congress had decided not to impose a common carrier obligation on the electric power industry and noted that the Commission was

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[199] *Id.* at p. 998.

[200] 410 U.S. 366 (1974).

[201] 410 U.S. at pp. 375-76.

not at that time expressly granted power to order wheeling.[202] In effect, it concluded that because Congress did not include common carrier provisions in the FPA, the Commission must not have any express authority to order wheeling that would preclude the District Court from imposing a wheeling remedy. Nowhere, however, did the Court say that the Commission lacked authority under section 206 to remedy undue discrimination. Indeed, that was simply not a matter before the Court or of any consequence to its decision.

In the FPA, while Congress elected not to impose common carrier status on the electric power industry, it tempered that determination by explicitly providing the Commission with the authority to eradicate undue discrimination -- one of the goals of common carriage regulation.[203] By providing this broad authority to the Commission, it assured itself that in preserving "the voluntary action of the utilities" it was not allowing this voluntary action to be unfettered. It would be far-reaching indeed to conclude that Otter Tail, which was a civil antitrust suit that raised issues entirely unrelated to our authority under section 206, is an impediment to our achieving one of the primary goals of the FPA -- eradicating undue discrimination in transmission in interstate commerce in the electric power industry.

In Richmond Power & Light Company v. FERC (Richmond),[204] the FPC, in reaction to the 1973 oil embargo,

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[202] *Id.* at pp. 374-76.

[203] *See AGD*, 824 F.2d at p. 998.

[204] 574 F.2d 610 (D.C. Cir. 1978).

was attempting to reduce dependence on oil. The FPC requested that utilities with excess capacity wheel power to the New England Power Pool (NEPOOL). In response, several suppliers and transmission owners filed rate schedules with the FPC that provided for voluntary wheeling. Richmond Power & Light Company (Richmond) objected to these filings, claiming that they were unreasonable because they did not guarantee transmission access. The FPC refused to compel the utilities to wheel Richmond's power, stating that it did not have the authority to order a public utility to act as a common carrier.

The D.C. Circuit upheld the Commission. It acknowledged that Richmond's argument was persuasive in some respects, **[31,671]** but stated that any conditions the Commission might impose could not contravene the FPA. The court examined the legislative history of the FPA and stated that "[i]f Congress had intended that utilities could inadvertently bootstrap themselves into common- carrier status by filing rates for voluntary service, it would not have bothered to reject mandatory wheeling * * *."[205]

However, the D.C. Circuit in no way indicated that the Commission was foreclosed from ordering transmission as a remedy for undue discrimination. Richmond also had argued that the alleged refusal of the American Electric Power Company (AEP) and its affiliate, Indiana & Michigan Electric Company (Indiana), to wheel Richmond's excess energy was unlawful discrimination because AEP and Indiana wheeled higher-priced electricity from other AEP affiliates. The court

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[205] *Id.* at p. 620.

acknowledged that Richmond's claim of unlawful discrimination was theoretically valid, but found that Richmond had failed to prove its case. It noted that if Richmond had argued that the rates were unjustifiably discriminatory, or that Indiana's failure to use its transmission capability fully or to purchase less expensive electricity for wheeling resulted in unnecessarily high rates, a different case would be before the court.[206] The case thus does not in any way limit the Commission's authority to remedy undue discrimination.

In Central Iowa Power Cooperative v. FERC,[207] the FPC[208] reviewed the terms of the Mid-Continent Area Power Pool (MAPP) Agreement under its section 205 and 206 authority. The agreement contained two membership limitations. First, the agreement established two classes of membership, with one class being entitled to more privileges than the other. Second, the agreement excluded non-generating distribution systems from pool services. The FPC found the first limitation on membership -- the two-class system -- to be unduly discriminatory and not reasonably related to MAPP's objectives. The FPC conditioned approval of the agreement under section 206 on the removal of the unduly discriminatory provision. The FPC found that the

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[206] *Id.* at p. 623, nn.53 and 57.

[207] 606 F.2d 1156 (D.C. Cir. 1979).

[208] While *Central Iowa* was pending, certain of the functions of the FPC were transferred to the FERC under the DOE Organization Act. Accordingly, the FERC was substituted for the FPC as the respondent in the case.

second limitation, the exclusion of non-generating distribution systems, was not anticompetitive and did not render the agreement inconsistent with the public interest.

On appeal, the D.C. Circuit affirmed the FPC's decision. The court found that the FPC did have authority to order changes in the scope of the MAPP agreement, if the agreement was unjust, unreasonable, unduly discriminatory or preferential under section 206 of the FPA. The court stated:

The Commission had authority, * * * under section 206 of the Act, * * * to order changes in the limited scope of the Agreement, including the addition of pool services, if, in the absence of such modifications, the Agreement presented "any rule, regulation, practice or contract (that was) unjust, unreasonable, unduly discriminatory or preferential."[209] However, the court agreed with the FPC's conclusion that the limited scope of MAPP was not unjust, unreasonable, or unduly discriminatory. The court recognized that a pool was not invalid under section 206 merely because a more comprehensive arrangement was possible.

The D.C. Circuit upheld the Commission's refusal to eliminate the second limitation on membership by ordering MAPP participants to wheel to non-generating electric systems.[210] However, neither the Commission nor the court was presented with the argument that wheeling was necessary as a remedy for undue discrimination.

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[209]606 F.2d at p. 1168.

[210]*Id.* at p. 1169; *see also Municipalities of Groton v. FERC*, 587 F.2d 1296 (D.C. Cir. 1978).

In Florida Power & Light Company v. FERC (Florida),[211] the Commission ordered Florida Power & Light Company (FP&L) to file a tariff setting forth FP&L's policy relating to the availability **[31,672]** of transmission service.[212] FP&L objected to including such a policy statement in its tariff and argued that the filing of such a policy would convert FP&L into a common carrier by obligating it to offer service to all customers.[213] There was no finding that the action ordered was necessary to remedy undue discrimination.

The Fifth Circuit Court of Appeals agreed with FP&L that the mandatory filing of the policy statement would require FP&L to provide transmission service beyond its voluntary commitment because such a requirement would

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[211]660 F.2d 668 (5th Cir. 1981), *cert. denied sub nom. Fort Pierce Utilities Authority v. FERC*, 459 U.S. 1156 (1983).

[212]FP&L provided transmission service when four conditions were met: (1) the specific potential seller and buyer were contractually identified; (2) the magnitude, time and duration of the transaction were specified prior to the commencement of the transmission; (3) it could be determined that the transmission capacity would be available for the term of the contract; and (4) the rate was sufficient to cover FP&L's costs.

[213]All utilities requesting wheeling services, subject to availability, would be entitled to receive transmission service under the filed terms. Any changes to a filed rate must be filed with the Commission. This is the so-called "filed rate doctrine." *See Northwestern Public Service Company v. Montana-Dakota Utilities Company*, 181 F.2d 19, 22 (8th Cir. 1980), aff'd, 341 U.S. 246 (1951).

change its duties and liabilities.[214] The Commission order would impose common carrier status on FP&L, the court found.[215] The court noted that the Commission did not rely on a finding of anticompetitive behavior and therefore the court did not address the Commission's power to remedy antitrust violations.[216]

The AGD court explicitly rejected the claim that the above line of cases establishes that the Commission lacks authority to require non-discriminatory open access.[217] Opponents of the Commission's order argued in AGD that Richmond and Florida, supra, stand for the proposition that the Commission cannot indirectly do what it allegedly cannot do directly, that is, impose common carriage. The AGD court

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[214]Under the filed rate doctrine, a refusal to wheel would be unduly discriminatory under section 206 of the FPA. As the court acknowledged, a customer refused service could petition the Commission to find that FP&L's policy of availability was unduly discriminatory under section 206(a) of the FPA. The court said that in the absence of a tariff on file, a utility refused wheeling services would be unable to claim discrimination under section 206(a) of the FPA. 660 F.2d at p. 675 (expressing "serious doubts that such a petition would be successful in the absence of a tariff").

[215]*Id.* at p. 676.

[216]*Id.* at p. 678.

[217]The AGD court did not address *New York State Electric & Gas Corporation v. FERC*, 638 F.2d 388 (2d Cir. 1980), cert. denied, 454 U.S. 821 (1981) (NYSEG), presumably because that case did not concern whether the Commission could order wheeling as a remedy for undue discrimination.

rejected these arguments, stating that the petitioners read the electric cases far too broadly:

(n)either Richmond nor Florida comes anywhere near stating that the Commission is barred from imposing an open-access condition in all circumstances.[218]

The court noted that the Florida case had expressly left open the question of whether the Commission would be entitled to use an open access condition as a remedy for anticompetitive conduct, and that in Richmond the D.C. Circuit had said little more than that unwillingness to transmit for all could not be automatically deemed undue discrimination. The court also noted the Central Iowa case, supra, in which it had upheld a Commission order that found a power pooling agreement discriminatory on its face because the agreement gave one class of membership privileged status over another. The court stated that the Central Iowa case "upholds the power of the Commission to subject approval of a set of voluntary transactions to a condition that providers open up the class of permissible users."[219] The court added that it refused to "turn statutory construction upside down" by letting Congress' failure to grant a general power of common carriage prevail over the affirmative grant of the specific power to eradicate undue discrimination.[220]

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[218]824 F.2d at p. 999

[219]*Id.* at p. 999.

[220]*Id.* at p. 1006.

We conclude that AGD's analysis of undue discrimination under sections 4 and 5 of the Natural Gas Act is equally applicable to an undue discrimination analysis under sections 205 and 206 of the **[31,673]** FPA. The Commission and courts have long recognized that the NGA was patterned after the FPA and that the two statutes should be interpreted in the same manner.[221] Thus, we conclude that we have the authority to remedy undue discrimination and anticompetitive effects by requiring all public utilities that own, control or operate transmission facilities to file non-discriminatory open access transmission tariffs.

b. Section 211 of the Federal Power Act

In concluding that we must invoke our section 206 authority to remedy undue discrimination and anticompetitive effects in the electric industry, we have carefully considered the goals of Title VII of the Energy Policy Act, and whether section 211 of the FPA, by itself, is sufficient to remedy undue discrimination in public utility transmission services. Title VII of the Energy Policy Act, which amended section 211 of the FPA to give the Commission broader authority to order wheeling in the public interest on a case-by-case basis, reflects the intent of Congress to encourage competitive wholesale electric markets. Section 211 provides a means for

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[221] *See, e.g., FPC v. Sierra Pacific Power Company*, 350 U.S. 348, 353 (1956); *Arkansas Louisiana Gas Company v. Hall*, 453 U.S. 571, 577 n.7 (1981); and *Kentucky Utilities Company v. FERC*, 760 F.2d 1321, 1325 n.6 (D.C. Cir. 1985). Section 206 of the FPA was recently revised and now differs from section 5 of the NGA, but not in a manner significant to our discussion here. See 16 U.S.C. 824e(b) and (c).

wholesale power sellers and buyers to obtain transmission services necessary to compete in, or to reach, competitive markets, and is a valuable tool to encourage competitive markets. However, in amending section 211, Congress left unaltered the authorities and obligations of the Commission under sections 205 and 206 (similar to our authorities and obligations under sections 4 and 5 of the NGA) to remedy undue discrimination. In addition, as discussed below, reliance on section 211 alone in some circumstances can result in the perpetuation of, rather than the elimination of, undue discrimination and anticompetitive effects.

First, there are inherent delays in the procedures for obtaining service under section 211. However, for competitive reasons, many transactions must be negotiated relatively quickly. Many competitive opportunities will be lost by the time the Commission can issue a final order under section 211. Case-by-case section 211 proceedings are not a substitute for tariffs of general applicability that permit timely, non-discriminatory access on request.

Second, discrimination is inherent in the current industry environment in which some customers and sellers are served by open access systems, and others have to rely on negotiated bilateral arrangements or the mandatory section 211 process. The end result is discrimination in the ability to obtain transmission services, as well as in the quality and prices of the services. This national patchwork of open and closed transmission systems, with disparate terms and conditions of service, cannot be cured effectively through section 211.

The Commission believes that its actions under sections 205 and 206 will complement the section 211 procedures to achieve both the Energy Policy Act's goals of creating more competitive bulk power markets and lower rates for consumers and the Federal Power Act's explicit direction in section 205(b) that no public utility shall, with respect to any transmission in interstate commerce, grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage.

2. Response to Commenters Opposing our Legal Authority

a. Authority to Order Open Access Tariffs

Initial Comments Supporting Commission Authority

A number of commenters support or state that they do not oppose the Commission's authority to order open access tariffs.[222] NIEP and CCEM explain that the AGD decision supports the Commission's action in this proceeding. ELCON asserts that the Commission's "extensive treatment of the relevant case law demonstrating FERC's authority to remedy this discrimination is legally sound." UtiliCorp argues that section 211 supports, rather than undermines, the Commission's **[31,674]** authority for the NOPR because it reflects Congress's intention to encourage more competitive bulk power markets.

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[222]NIEP, ELCON, CINergy, UtiliCorp, TAPS, SBA, Entergy, NY Energy Buyers, Sierra.

Initial Comments Opposing Commission Authority

Other commenters assert that the Commission has improperly relied on sections 205 and 206 of the FPA to require open access.[223] They argue, for instance, that Otter Tail should be read as a broad constraint on the Commission's authority to order wheeling for any purpose and that the AGD decision does not undermine that holding or the cases following Otter Tail.[224] In support, some of these commenters discuss Richmond Power & Light, New York State Electric & Gas Corporation, and Florida Power & Light Company, the same cases discussed by the Commission in the NOPR.[225]

For example, EEI highlights the AGD court's discussion noting the difference between the legislative history of the NGA and that of the FPA, which the court stated was not as strong as that of the NGA. Moreover, EEI argues that the court found that section 7 of the NGA provided support for the Commission's actions in Order No. 436 and that such section 7 conditioning authority is lacking under the FPA. Allegheny notes that AGD did not overrule Otter Tail. Dayton P&L states that, in the gas case, the Commission was

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[223]*E.g.*, EEI, Atlantic City, Allegheny, VA Com, PA Com, Ohio Edison, Southern, Utilities For Improved Transition, Dayton P&L, SCE&G, Centerior, BG&E, Central Hudson, NY Com, Salt River, Carolina P&L, Union Electric, VEPCO, Utility Workers Union.

[224]EEI, VA Com, Union Electric.

[225]E.g., EEI, VA Com, NY Com, PA Com, Salt River, Southern, Dayton P&L, Detroit Edison, BG&E.

responding to voluntary filings by pipelines. It also says that before the NOPR, the Commission itself saw its authority as more limited. SCE&G points to differences between Commission jurisdiction over public utilities and gas pipelines and criticizes the Commission's alleged assumption that the circumstances involved in the gas and electric industries are virtually identical.

PA Com argues that the attempt to analogize to the NGA and the cases that refer to that Act is inconsistent with the technical and engineering realities of the electric transmission grid and that extensive comparisons between the natural gas industry and the electric industry are misleading.[226]

FL Com argues that, in relying on sections 205 and 206 to establish generic open access transmission tariffs for all public utilities, the Commission violates the court's decision in Cajun Electric Power Cooperative v. FERC, 28 F.3d 173 at 179 (D.C. Cir. 1994), where, FL Com argues, the court refused to allow the Commission to use a non-evidentiary ruling when there were material facts at issue.

Reply Comments

CCEM responds that EEI and others confuse the obligations of a common carrier with the duty of public utilities not to unduly discriminate. It says that AGD supports the Commission's authority because the legislative history of

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[226]See also NY Com (NGA has no parallel provision to section 211 of the FPA), Salt River.

the FPA and the NGA are similar with respect to common carriage. According to CCEM, early versions of both statutes would have made the regulated industries operate as common carriers (citing Otter Tail, the legislative history of the FPA, the legislative history of the Public Utility Holding Company Act, and the legislative history of the Mineral Leasing Act), but that Congress chose not to impose the common carrier obligations.

CCEM also says that the duties the Commission imposed on the gas industry and those in the NOPR are not common carriage in any event. According to CCEM, a common carrier must carry all goods offered (citing Am. Trucking Assoc. v. Atchison, T. & S.F. Ry. Co., 387 U.S. 397, 406 (1967)). Finally, CCEM cites Stephenson v. Binford, 287 U.S. 251, 265-66 (1932), where the Supreme Court held that obligations that are typical of common carriers can be imposed on contract motor carriers.

CCEM further disagrees with EEI's argument that the enactment of section 211 was a disavowal of any other Commission authority to order transmission.

[31,675]

ELCON also disagrees with EEI's claim that the Energy Policy Act undermines the Commission's pre-existing section 205 and 206 authority. It states that the savings clause in section 212(e) of the FPA, as amended, explicitly expresses Congress' intention not to undermine the Commission's pre-existing authority and that the legislative history contains nothing to suggest otherwise.

Similarly, in response to those who argue that section 211 is the only source of authority for the Commission to order transmission, NIEP argues that sections 211 and 212 serve purposes different from section 206. It says that the Commission's authority to order transmission in the "public interest" under sections 211 and 212 is not synonymous with its authority to order transmission as a remedy for undue discrimination under section 206; the two standards are complementary but distinct:

> Although broadly applicable, the Commission's ability to order wheeling under Sections 211 and 212 is carefully limited by a number of procedural provisions. Foremost among these is the requirement that the wheeling may be ordered only upon a specific application for transmission services. FERC's authority to act in the public interest is thus confined to the individual case.
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> By contrast, FERC's remedial powers under Section 206 can be exercised upon a finding of unjust, unreasonable or unduly discriminatory or preferential practices. Once that finding has been made, however, the form and substance of the remedy is left entirely to the FERC's discretion. If FERC deems it necessary, FERC may adopt generally applicable rules or practices as a countermeasure to discriminatory acts, including ordering utilities to file generally applicable transmission tariffs.[227]

NIEP also points out that the legislative history does not address the Commission's authority to order transmission

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[227]NIEP Reply Comments at p. 8.

as a remedy for undue discrimination. It challenges the interpretation of the legislative history advanced by some commenters.[228]

Next, NIEP defends the Commission's proposed findings that there is generally undue discrimination in the provision of transmission service. It notes that when an agency acts on an industry-wide basis, the agency does not have to make a finding as to each particular case.

Finally, NIEP responds to those who argue that AGD is not on point. It notes that the AGD court discussed electric cases and emphasizes the court's statement that the NGA "fairly bristles with concern for undue discrimination" -- a statement that is equally true of the FPA.

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[228]NIEP explains that

> (W)hile much has been made of the Senate report accompanying S.2114, which subsequently became part of PURPA in 1978, that report does not illustrate an intent to limit FERC's authority to remedy undue discrimination under Section 206. That report characterizes the Supreme Court's decision in Otter Tail as holding that "the Federal Power Act leaves open a gap in its failure to assign the FPC general authority to order wheeling in this situation * * *." The "situation" to which the Report refers is not discrimination, however. Instead, the statement appears to make reference to circumstances in which general public interest concerns, such as reliability, efficiency and competition, are at stake. Thus, Senate Report 2114 is simply not a limitation on the Commission's remedial powers under Sections 206.
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> NIEP Reply Comments at p. 8-9 (citations omitted).

TDU Systems responds to the argument that Otter Tail is a broad constraint on the Commission's authority to order transmission.[229] At issue in that case, it argues, was the reach of the Sherman Act, not of FPA sections 205 and 206. Similarly, it argues, the Florida Power case is not on point, and the court there specifically said that it was not deciding whether the Commission could have ordered wheeling as a remedy for anticompetitive activities. Moreover, TDU Systems asserts that EEI's use of a quote from a single Senator should carry no weight, since it is a well-established principle of statutory construction that such statements have little value. Finally, it points out that the AGD court itself did not view Otter Tail or other electric precedent as forbidding the Commission to order wheeling as a remedy for undue discrimination.

[31,676]

Entergy asserts that Congress's refusal to require utilities to provide transmission as common carriers or whenever it is in the public interest was merely a decision not to give the Commission general authority to order wheeling, without regard to undue discrimination. Thus, the Otter Tail language concerning the absence of a common carrier requirement does not demonstrate that Congress meant to limit the Commission's authority to remedy undue discrimination.

ELCON disputes EEI's reading of NYSEG, noting that the NYSEG court explicitly stated:

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[229]See also Entergy.

Nor do we suggest that the Commission is powerless to review a wheeling agreement under 206 without following the requirements of sections 211 and 212.[230]

TAPS discusses numerous cases, including the primary cases relied upon by the Commission, and disposes of NYSEG by stating that it is no longer good law, if it ever was.

Commission Conclusion

There can be no question that the Commission has the authority to remedy undue discrimination. Sections 205 and 206 of the FPA mandate that we ensure that, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, no person is subject to any undue prejudice or disadvantage. Under these sections, we must determine whether any rule, regulation, practice, or contract affecting rates for such transmission or sale for resale is unduly discriminatory or preferential, and we must disapprove those contracts and practices that do not meet this standard. Our discretion is at its zenith in fashioning remedies for undue discrimination.[231]

Some commenters, however, challenge our authority to order industry-wide non-discriminatory open access as a remedy for the undue discrimination we have found in the

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[230]ELCON Initial Comments at p. 7 (quoting NYSEG at 403).

[231]See, *e.g.*, Niagara Mohawk Power Corporation v. FPC, 379 F.2d 153, 159 (D.C. Cir. 1967).

industry. As summarized above, they essentially assert that we are prohibited by court precedent, the legislative history of the FPA, and sections 211 and 212 of the FPA from ordering wheeling as a remedy for undue discrimination. We disagree and conclude that we have the authority -- indeed, a responsibility -- to require non-discriminatory open access transmission as a remedy for undue discrimination.

AGD and Legislative History

The court decision in Associated Gas Distributors v. FERC provides powerful support for our ability to order industry-wide non-discriminatory open access transmission in the electric industry as a remedy for undue discrimination. As discussed in detail above, AGD, which is the only decision to have addressed the Commission's authority to remedy undue discrimination by requiring open access, upheld our authority under section 5 of the NGA (the parallel to section 206 of the FPA) to require open access in the natural gas industry. The rationale supplied by the AGD court applies equally to the FPA and our responsibility to eliminate undue discrimination in the electric industry.

Those who challenge the Commission's legal authority to remedy undue discrimination face the same difficulty that parties faced in seeking to overturn open access in the natural gas industry -- they "can point to no language in the (FPA) barring the Commission from imposing common carrier status on (public utilities), and certainly none barring it from imposing upon the (public utilities) a specific duty that happens to be a typical or even core component of such

status."[232] Instead, as was unsuccessfully attempted in the AGD proceeding, they seek to overcome the statutory silence primarily by means of legislative history. However, as the AGD court explained, legislative history is not even relevant, because

courts have no authority to enforce principles gleaned solely from legislative history that has no statutory reference point.[233] Here, as the court found with respect to the NGA, the legislative history of the FPA "provides strong support only for the point that Congress declined itself to impose common carrier status on (public utilities) * * * It affords weak -- **[31,677]** almost invisible -- support for the idea that the Commission could under no circumstances whatsoever impose obligations encompassing the core of a common carriage duty."[234]

Commenters focus on the following statement in the AGD decision to support the argument that, because Congress did not expressly reject common carriage under the NGA, but did reject it under the FPA, a different outcome in this proceeding is required:

we note that the legislative history of the two acts is, on this point, materially different. In its deliberations on the bill that

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[232]AGD, 824 F.2d at 997.

[233]*Id.* (quoting IBEW, Local No. 474 v. NLRB, 814 F.2d 697, 712 (D.C. Cir. 1987)(emphasis deleted by court from original)).

[234]*Id.* (emphasis added).

ultimately emerged as the Federal Power Act, Congress considered and rejected a provision that would have "empowered the Federal Power Commission to order wheeling if it found such action to be 'necessary or desirable in the public interest.'" (citing Otter Tail) (quoting S. 1725, 74th Cong., 1st Sess.). The evidence as to the NGA (surveyed above) is less direct: it consists exclusively of various occasions on which Congress did not adopt proposals actually making the natural gas pipelines into common carriers.[235]

The above statement, however, does not preclude the AGD court's decision on our broad authority to remedy undue discrimination in the gas industry from applying equally in the electric industry. Clearly, the court did not say that. As discussed below, we believe the statement focuses on a distinction in the legislative histories that is not meaningful.

First, whether or not a material difference exists in the respective legislative histories of the NGA and FPA, the fact remains that the crucial findings of the AGD court were that: (1) "Congress declined itself to impose common carrier status" (emphasis added) and (2) there is no "support for the idea that the Commission could under no circumstances whatsoever impose obligations encompassing the core of a common carriage duty."[236] These findings apply equally to the

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[235] *Id.* at p. 998-99.

[236] *Id.* at p. 997. We also note that the contract carriage obligation we are imposing is easily distinguished from the common carrier obligation Congress chose not to adopt. As discussed infra, the common carrier provisions rejected by Congress would have required transmission for "any person" upon reasonable request.

FPA. Simply stated, statutory silence cannot be overcome by means of legislative history -- even if the legislative history in fact indicated that Congress "rejected" legislative imposition of common carrier status under the FPA, but "did not adopt" it under the NGA. In either event, nothing in the statute or legislative history suggests that Congress concluded that the Commission could under no circumstances impose open access as a remedy to undue discrimination.

Moreover, the legislative history of the bills containing the FPA and the NGA, taken as a whole, suggests that the distinction drawn in AGD between the legislative histories of the NGA and the FPA is not meaningful. The legislation that was to become the FPA originally included provisions regulating both electric power and natural gas. As originally proposed, the legislation contained identical common carriage language for both public utilities and natural gas pipelines.

With respect to the FPA, the Supreme Court explained in Otter Tail that (a)s originally conceived, Part II would have included a "common carrier" provision making it "the duty of every public utility to * * * transmit energy for any person upon reasonable request * * *." In addition, it would have empowered the Federal Power Commission to order wheeling if it found such action to be "necessary or desirable in the public interest." H.R. 5423, 74th Cong., 1st Sess.; S. 1725, 74th Cong. 1st Sess. These provisions were eliminated to preserve "the voluntary action of the utilities." S.Rep. No.

This would have included retail purchasers.

621, 74th Cong., 1st Sess., 19.[237] The language paraphrased by the Supreme Court was from Title II of the initial bill proposing the Public Utility Holding Company Act. The entire sections from which the paraphrased language came are as follows:

SEC. 202. (a) It shall be the duty of every public utility to furnish energy to, exchange energy with, and transmit energy for any person upon reasonable request therefor; and to furnish and maintain such services and facilities as **[31,678]** shall promote the safety, comfort, and convenience of all its customers, employees, and the public, and shall be in all respects adequate, efficient, and reasonable.

* * *

SEC. 203. (b) Whenever the Commission after notice and opportunity for hearing finds such action necessary or desirable in the public interest, it may by order direct a public utility to make additions, extensions, repairs, or improvements to or changes in its facilities, to establish physical connection with the facilities of one or more other persons, to permit the use of its facilities by one or more other persons, or to utilize the facilities of, sell energy to, purchase energy from, transmit energy for, or exchange energy with, one or more other persons. Where any such order affects two or more persons, the Commission may prescribe the terms and conditions of the arrangement to be made between such persons, including the apportionment of

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[237]Otter Tail, 410 U.S. at p. 374.

cost between them and the compensation or reimbursement reasonably due to any of them.[238]

This initial bill proposing the Public Utility Holding Company Act also included a Title III that was intended to regulate the transmission and sale of natural gas. Sections 303(a) and 304 of Title III included the identical common carrier language paraphrased by the Supreme Court and included in sections 202(a) and 203(b) of Title II.[239] After further deliberations, Congress rejected the above-quoted language in Title II and eventually adopted a Title II that did not include any common carrier language. On the other hand, Title III (addressing regulation of natural gas) was not reported out of committee, but reemerged in the next year.[240]

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[238]H.R. 5423, 74th Cong., 1st Sess., 32 (emphasis added).

[239]*Id.* at p. 44.

[240]In the debate on the subsequent bill to regulate natural gas, Congressman Cole explained:

Mr. Chairman, the House should realize that the measure we are dealing with today is of extreme importance, more so than the attendance and the time taken in the discussion would seem to indicate. It is the culmination of one of the most far-reaching, intensive studies of the Federal Trade Commission I assume that that Commission ever conducted, and last year found a place in not identical language but very similar in the Rayburn bill, the famous holding-company bill, as part 3 thereof. Our committee eliminated part 3, as members will recall, and saved it for a separate measure reported out as it was last year, which was not considered by the House, but is here today in improved form. 81 Cong. Rec. H6724 (daily ed. July 1, 1937).

The bill that reemerged did not contain the common carrier language that was in the original Title III. However, as Congress had just debated the common carrier issue in enacting electric power regulation, it is not surprising that Congress did not engage in debating the very same issue in enacting natural gas regulation.

Because of the timing of the legislation involving the FPA and the NGA and the logical nexus between the two acts, we conclude that there is in fact no material difference as to this issue in the legislative histories of the two acts. Both initially included identical common carrier language, and the language was removed from both. As to both acts, Congress chose not to impose common carrier obligations on the electric or natural gas industries, but gave the Commission the authority and responsibility to eliminate undue discrimination in both industries. Consequently, as open access was found to be a proper remedy for undue discrimination in the natural gas industry, it is also a proper remedy for undue discrimination in the electric industry.

As the AGD court noted with respect to the Commission's powers and duties under the NGA, Congress explicitly gave the Commission the authority to eradicate undue discrimination under the FPA. That explicit power and duty provided by Congress cannot be invalidated solely on the ground that Congress chose not to impose statutory common carrier status on public utilities or did not explicitly authorize the Commission to do so.[241] As the AGD court explained, this would "turn[] statutory construction upside down, letting the

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[241] AGD, 824 F.2d at p. 998.

failure to grant a general power prevail over the affirmative grant of a specific one."[242]

[31,679]
Other Case Law

A number of commenters argue that the Commission misinterpreted the other cases discussed in the NOPR with respect to our authority to order non-discriminatory open access transmission. We disagree. As demonstrated above, not one of the cases put forth by commenters holds that we cannot remedy undue discrimination by requiring public utilities to provide non-discriminatory open access transmission.[243]

AGD is the only case in which a court specifically addressed our authority to order open access transmission as a remedy for undue discrimination. Its favorable finding with respect to our action under section 5 of the NGA directly supports our ordering non-discriminatory open access transmission under section 206 of the FPA. Authority to Act by Rule

We disagree with those commenters that assert that we may find and remedy undue discrimination only through case-

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[242] *Id.*

[243] See *FERC Statutes and Regulations* at p. 33,053-56. We further note that the AGD court did not discuss the NYSEG decision at all. Indeed, the NYSEG case did not involve any allegations of undue discrimination and any discussion of section 206 by the court was dictum.

by-case adjudications and are prohibited from making a generic determination of undue discrimination through a rulemaking. First, there is no question that it is within our discretion whether we act through rule or through case-by-case adjudications.[244] The AGD court specifically rejected a similar argument that the Commission erred in requiring open access transportation tariffs without first finding that each individual pipeline's rates were unlawful. The AGD court held that "(t)he Commission is not required to make individual findings if it exercises its §5 authority by means of a generic rule."[245]

We have identified a fundamental generic problem in the electric industry: owners, controllers and operators of monopoly transmission facilities that also own power generation facilities have the incentive to engage, and have engaged, in unduly discriminatory practices in the provision of transmission services by denying to third parties transmission services that are comparable to the transmission services that they are providing, or are capable of providing, for their own power sales and purchases. These practices

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[244]*See, e.g., NLRB v. Bell Aerospace Company*, 416 U.S. 267, 293 (1974) (citing *SEC v. Chenery Corporation*, 332 U.S. 194, 202-03 (1947). *See also Heckler v. Campbell*, 461 U.S. 458, 467 (1983) (even where enabling statute requires a hearing to be held, agency may rely on its rulemaking authority); *Panhandle Eastern Pipeline Company v. FERC*, 907 F.2d 185, 187-88 (D.C. Cir. 1990). Under section 403 of the DOE Act, 42 U.S.C. 7173, the Commission is authorized at its discretion to initiate rulemaking proceedings.

[245]AGD, 824 F.2d at p. 1008.

drive up the price of electricity and hurt consumers. Furthermore, the incentive to engage in such practices is increasing significantly as competitive pressures grow in the industry. It is within our discretion to conclude that a generic rulemaking, not case-by-case adjudications, is the most efficient approach to take to resolve the industry-wide problem facing us.

b. Undue Discrimination/Anticompetitive Effects Initial Comments

A number of commenters allege that the Commission has failed to meet its burden of proving industry-wide discrimination.[246] They assert that the Commission has provided only a few unsubstantiated allegations of discrimination, which do not represent the current conditions in the electric industry, or that the Commission has not shown that all electric utilities have unduly discriminated. Some attack the NOPR's incorporation by reference of the unsubstantiated allegations of discrimination set forth in a petition for rulemaking filed on February 16, 1995 by the Coalition for a Competitive Electric Market (CCEM).[247]

EEI argues that the allegations of discrimination in the NOPR must be considered in light of the fact that: (1) all tariffs currently on file have been found by the Commission not to be discriminatory; (2) more than 30 utilities have voluntarily filed open access tariffs, which belies any

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[246]E.g., EEI, Ohio Edison, PA Com, BG&E, NY Com, Minnesota P&L, Carolina P&L.

[247]E.g., EEI, BG&E.

assertion of widespread discrimination in the industry; and (3) transmission disputes are rare, with only 19 **[31,680]** section 211 proceedings having been filed in the last three years.[248] EEI concludes that the Commission's allegations of discrimination do not rise to the level of "extreme circumstances" found by the court in the natural gas industry in AGD.

EEI adds that the Commission's proposal to act under section 206 is itself discriminatory because it applies only to public utilities and does not reach all transmission-owning utilities.[249] If reciprocity is designed to resolve this problem, EEI believes that reciprocity should also be "effective for public utilities." Furthermore, EEI argues that the failure of a public utility to provide to others a service that it does not provide itself is not evidence of discrimination, and that inclusion of such a provision actually results in preferential treatment for transmission users.

NE Public Power District alleges that the NOPR does not contain a single reference to any actual discrimination or anticompetitive conduct by any publicly owned utility.

Salt River asserts that the Commission is required to consider all elements of an antitrust analysis before reaching a conclusion that market power exists in the transmission

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[248]See also Ohio Edison.

[249]See also SCE&G.

system and that we have failed to do so.[250] It concludes that the NOPR "constitutes an attempt to legislate a remedy for an evil that has not been, and cannot be, lawfully found to exist on a wholesale basis among utilities that own and operate integrated generation and transmission systems."[251]

PA Com argues that the Commission's request for examples of discriminatory behavior is a "tacit admission as to the paucity of evidence of discriminatory practices by transmission owning utilities." NY Com argues that the "Commission's lack of a record basis for its proposed findings is legally suspect because courts in two cases have held that the Commission cannot proceed with open access transmission tariffs absent record findings of specific anticompetitive conduct."[252]

Finally, EEI claims that even if the Commission has proven its allegations of discrimination, we have failed to meet the requirements of section 206 of the FPA.[253] According to EEI, the Commission cannot find, without an adjudicatory hearing, that the rates on file are unlawful and

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[250]Salt River Initial Comments at p. 5-6 (referencing an attached legal memorandum of Donald A. Kaplan).

[251]Salt River Initial Comments at p. 6.

[252]NY Com Initial Comments at p. 1 FLA-PAGE CITIATION ?6-18 (discussing FPL and Cajun).

[253]See also Southern.

order replacement rates.[254] The Commission's proposed procedure would unlawfully place the burden of justifying existing rates on the utilities.

Reply Comments

A number of commenters provide instances of discriminatory behavior they have faced over the years. NCMPA describes difficulties it has faced in dealing with CP&L, including a situation where CP&L allegedly impeded NCMPA's use of transmission access through CP&L's control of dispatching.[255]

AMP-Ohio alleges that Toledo Edison refused to transmit emergency power on a buy-sell basis to certain AMP-Ohio members even though Toledo Edison's system was not constrained. Instead, AMP-Ohio alleges, Toledo Edison bought the power and resold it to AMP-Ohio at a higher rate.

APPA challenges EEI's claim that there is no substantial evidence of undue discrimination in transmission. It suggests that nineteen instances of transmission disputes being filed since the Energy Policy Act was enacted is ample evidence of undue discrimination. Moreover, according to APPA, reported abuses are only the tip of the iceberg.

CCEM responds to the argument raised by EEI and others that there is no showing of extreme circumstances of

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[254]See also Southern.

[255]We note that CP&L raised legal objections to our authority to implement this rule.

discrimination in the electric industry such as the AGD court noted in the gas industry. It says that these circumstances are present and gives numerous examples; it does not identify the specific utilities because "it is the experience of * * * (our) members that nearly all transmission owners retaliate **[31,681]** * * *" against anyone who complains. Moreover, in answer to EEI's statement that transmission disputes are rare, CCEM states that since most of the competition is in the short-term market, it has not been worthwhile to file complaints. The examples provided by CCEM include: (1) refusal by a California public utility to offer firm service; (2) refusal by control area utilities in Texas to offer ancillary services to a power marketer, with the result that one of the utilities won the bid, even though it did not have the lowest price; (3) non-utilities in ERCOT being unable to compete to meet short-term requests for economy energy because they were required to schedule by noon of the preceding day, while utilities did not subject themselves to such a scheduling requirement; (4) power pool or control area information requirements, particularly in the northwest part of WSPP, that force non-utilities to reveal commercially sensitive information; the transportation operator has then revealed the information to its own or its affiliate's sales arm, which "steals" the deal; (5) a northeast power pool that refused to wheel out even though capacity was available on the grounds that sending power out of the pool would drive up prices in the pool (hoarding); (6) a power marketer that asked a utility to provide transmission, whereupon the utility bought up certain transmission capacity necessary for the marketer to reach its buyer, thus blocking the path -- this was possible because the utility was able to locate the purchaser based on commercially sensitive information the marketer had to give the utility when the marketer asked for transmission; (7) a common contracting

practice among utilities restricting the use of interconnections to themselves, particularly in the Southwest Power Pool, MAPP, and MAIN; (8) utilities overstating the cost of improvements (gold-plating) and thus discouraging service. CCEM also responds to each of EEI's criticisms of CCEM's examples of undue discrimination submitted in its February 16, 1995 petition and argues that its examples of undue discrimination are unrebutted.

Brownsville asserts that

while PUB [Brownsville] must pay multiple distance-based and pancaked transmission rates to engage in transactions with the non-ERCOT universe, El Paso Electric would have received transmission payments from its merger partners while gaining free transmission access to buy and sell within ERCOT. CSW presently walls other ERCOT utilities off from participation in the Western Systems Power Pool, while its ERCOT subsidiaries, CPL and WTU, share in the benefits of their non-ERCOT affiliates' WSPP memberships via the preferential terms of the CSW Operating Agreement. CSW treats its own inter-affiliate central dispatch as having a higher priority than third-party economy energy transactions, with the result that CPL not infrequently crowds PUB out of the economy market.[256]

Wisconsin Municipals states that its members have been fighting transmission battles for years and sets forth five examples of the sort of difficulties it has experienced in

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[256]Brownsville Reply Comments at p. 2-3 (emphasis in original).

attempting to obtain transmission rights. For example, it explains that Wisconsin public utilities have resisted an effort by the state commission to achieve comparability of use of transmission. Wisconsin Municipals also explains a situation where "if WPPI continued to purchase its power from WPSC, it would pay WPSC $843,840 annually for transmission service: if it purchases power off system from WP&L (one of WPSC's competitors), WPPI would pay WPSC $1,774,224 for transmission service to the exact same load."

TAPS sets forth additional examples of undue discrimination, including refusals to wheel even in the face of Nuclear Regulatory Commission (NRC) nuclear license conditions requiring wheeling, and Northeast Utilities' refusal to provide transmission to a QF even though it had indicated to the Commission that it would provide such transmission in order to obtain Commission approval of its proposed merger with Public Service Company of New Hampshire.

NIEP sets forth ten examples of undue discrimination that its members have experienced in seeking access to transmission service at reasonable terms and conditions.

[31,682]

Some commenters challenge these claims of undue discrimination. For example, Carolina P&L responds to NCMPA #1's example of obstruction by Duke in accommodating energy sales from the jointly owned Catawba Plant. Carolina P&L explains that NCMPA #1's proposal "would require Duke to provide its own generation resources on behalf of NCMPA #1 in order to support a bulk power sale when NCMPA #1's own resource capacity and energy are not sufficient for the sale." Carolina P&L argues that this is

backstanding that goes beyond the scope of any ancillary service the Commission has proposed and would be entirely inappropriate "to compel the Transmission Provider to sell power to its Transmission Customer for resale on the bulk power market."

Duke also responds to NCMPA #1's claim of discrimination and asserts that NCMPA #1's claim is not relevant to the NOPR proceeding, but is a specific contractual claim that should be pursued pursuant to the terms of its contract.

Commission Conclusion

We conclude that unduly discriminatory and anticompetitive practices exist today in the electric industry and, more importantly, that such practices will increase as competitive pressures continue to grow in the industry, unless the Commission acts now to prevent such practices.[257] It is in the economic self-interest of transmission monopolists, particularly those with high-cost generation assets, to deny transmission or to offer transmission on a basis that is inferior to that which they provide themselves. The inherent characteristics of monopolists make it inevitable that they will act in their own self-interest to the detriment of others by refusing transmission and/or providing inferior transmission to competitors in the bulk power markets to favor their own

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[257]While many public utilities have filed some form of open access tariff (often in response to our proposed rule), we believe that many of the remaining utilities will not voluntarily open their systems absent a final rule. See also note 266.

generation, and it is our duty to eradicate unduly discriminatory practices. As the AGD court stated: "Agencies do not need to conduct experiments in order to rely on the prediction that an unsupported stone will fall."[258]

We set forth examples in the NOPR of undue discrimination that we believe are occurring in the electric industry and invited commenters to identify any discrimination that they may have experienced. In response, commenters presented numerous additional examples of undue discrimination, which are summarized above, and we set forth below further examples of undue discrimination that have been raised in cases before the Commission.

Many of the examples of discriminatory behavior that have been brought to our attention do not name the specific utilities involved, and many are allegations that are not proven. However, we do not believe that this undermines our finding of unduly discriminatory practices by transmission owners and controllers. We believe that it is only natural that potential transmission customers with an interest in participating in electric markets will be reluctant to name names for fear of being shut out of those markets. CCEM, which identified a wide array of discriminatory behavior its members have experienced, explained that

(w)e do not identify the specific utilities in each example because it is the experience of CCEM members that nearly all transmission owners retaliate by cutting off all communications with anyone that challenges or complains

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[258]AGD, 824 F.2d at p. 1008.

about the rates, terms or conditions at which the owner offers access to its system. Inasmuch as most of the competitive commerce in electric power today is in short-term markets, it is typically not worth the effort of CCEM members or other transmission-dependent entities to file a complaint with the Commission's enforcement staff or in the courts in connection with a transmission owner's discriminatory practices. The deal is lost well before a complaint can be processed and ruled upon.[259]

Other examples of discriminatory behavior have also been raised in proceedings before the Commission. As we **[31,683]** explained in detail in the NOPR, transmission-owning utilities have discriminated against others seeking transmission access in a variety of ways, most often subtly and indirectly.[260] For example, delaying tactics have been used to frustrate access. The history of Pacific Gas and Electric Company's (PG&E) attempt to avoid its commitments made to the California owners of the California-Oregon Transmission Project (COTP) is a prime example. The owners had originally planned the COTP to have its southern terminus at the Midway station with Southern California Edison. PG&E convinced them to terminate the project instead at PG&E's Tesla station and indicated that PG&E would provide transmission service the rest of the way south to Midway. PG&E promised this service in 1989 (in Principles). PG&E spent the next four years filing substitute

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[259]CCEM Initial Comments at p. 18-19. See also NIEP Reply Comments at p. 13 n.31.

[260]*FERC Statutes and Regulations* at p. 33,072.

provisions for what it had promised in the Principles.[261] Additional allegations of discriminatory behavior are set forth in Appendix C, which includes allegations made under oath in proceedings at the Commission and allegations made in pleadings and other documents before the Commission.

In addition, to date, the Commission has received 28 section 211 transmission requests.[262] Applicants submit section 211 transmission requests when the transmission provider refuses to provide the requested transmission service. For example, American Municipal Power-Ohio, Inc. (AMP-Ohio) requested Ohio Edison Company (Ohio Edison) to establish additional delivery points to certain of AMP-Ohio's members and to permit the addition of delivery points in the future upon AMP-Ohio's request. Ohio Edison refused AMP-Ohio's request, claiming that it was not a proper request under section 211 because it already provided wholesale transmission to the municipal utilities at issue. In a proposed order, the Commission disagreed with Ohio Edison and ordered Ohio Edison to provide the requested additional

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[261] *See Pacific Gas and Electric Company*, 65 FERC ¶61,312 at p. 62,428-30 and n.22, remanded on other grounds, *Pacific Gas & Electric Company v. FERC*, No. 94-70037 (9th Cir. June 23, 1994)(unpublished opinion), order on remand, 69 FERC 61,006 (1994).

[262] A list of section 211 applications and the status of each is attached as Appendix A.

delivery points and to entertain future requests by AMP-Ohio for specific delivery points.[263]

Many of the examples of discriminatory actions we are seeing in the electric industry are similar to those we saw in the gas industry. Given our experience, we find that these examples of discriminatory actions are credible and well-founded. Thus, we conclude that there is more than sufficient reason to believe that transmission monopolists currently engage in unduly discriminatory practices, and that they will continue to engage in unduly discriminatory practices, unless we fashion a remedy to eliminate their ability and incentive to do so. In light of the competitive changes occurring in today's electric industry, we believe that the only effective remedy is non-discriminatory open access transmission, including functional unbundling and OASIS requirements, and that it is within our statutory authority to order that remedy.

Further, we disagree with the argument that we are limited to applying a traditional antitrust analysis in determining whether market power exists in the transmission system. While we must take antitrust concerns into consideration in exercising our responsibilities under the FPA, we are not an antitrust court, and our responsibilities are not those of the Department of Justice.[264] We have

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[263] *American Municipal Power-Ohio, Inc. v. Ohio Edison Company*, 74 FERC ¶61,086 (1996).

[264] *See, e.g., Gulf States Utilities Company v. FPC*, 411 U.S. 747, 758-60 (1973); *FPC v. Conway Corporation*, 426 U.S. 271, 279 (1976); *Northern Natural Gas Company v. FPC*, 399 F.2d 953, 960 (D.C. Cir. 1968).

analyzed the incentives and practices of monopoly transmission owners and controllers in light of the statutory standards and directives of the FPA and, based on our findings, have properly concluded that there is a generic problem that must be remedied.

The Commission also recognizes, as some commenters suggest, that we have, in the past, permitted utilities to file tariffs containing restrictions on transmission **[31,684]** service that we are now finding to be unduly discriminatory in this rule and that we found unduly discriminatory in cases since our decision in AEP. However, it is entirely appropriate, and indeed necessary, that our application of the FPA's undue discrimination standard evolve over time and adapt to the changing circumstances in the industry. Our prior willingness to tolerate the use of monopoly power over transmission to maintain and aggregate the utility's market power over generation occurred in the context of an industry structured largely as vertically integrated regulated monopolies that supplied all facets of utility service -- power supply, transmission, and distribution -- as a single monopoly service. Competition generally was not meaningfully available as a means to discipline prices and consumer interests were best served by improving efficiencies of the integrated utilities, subject to cost-based regulation.

Today, the circumstances of the industry are radically different. As explained in detail in Section III, a series of significant economic, regulatory, and technical changes in the power industry has introduced the promise of competitively priced power supplies. The profile of electric power suppliers has expanded to include not just the power supply arms of traditional utilities, but also independent power suppliers,

affiliated utility power suppliers selling into territories of other franchise utilities, and power marketers.[265] This offers the promise of an increasingly competitive commodity market in electric power, in which significant benefits to consumers can be achieved. In the context of an emerging competitive market in generation, discriminatory practices that once did not constitute undue discrimination must be reviewed to determine whether they are being used to prevent the benefits of competition in generation from being achieved. Here we find conclusively that they are, and use our remedial authority to ensure that they can no longer occur.[266]

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[265]We note that there are now 14 power marketers that are affiliated with public utilities.

[266]We take note of EEI's comments that, at the time of the comments, 30 utilities had filed open access tariffs. They argue, therefore, that the rule is unnecessary. Since their comment was filed, the number of utilities filing some form of an open access tariff has risen to 106. However, while some of these tariffs are based on the NOPR pro forma tariffs, many of these tariffs fall significantly short of the tariff requirements of both the NOPR and this Rule. Even if the tariffs met these requirements, the Rule is still needed to complete the task of eliminating undue discrimination by all public utilities and assuring, to the extent possible, a nationwide open access transmission grid. Indeed, a number of these tariffs were filed for the purposes of securing authority to market power competitively. This underscores markedly our fundamental conclusion that prior practices of using monopoly power over transmission to preserve market power over electricity sales has no place in today's industry and must be eliminated to get the benefits of competition to the customers we are required to protect under the FPA.

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[pp. 31,687 - 31,703]

[31,687]

C. *Comparability*

1. Eligibility to Receive Non-Discriminatory Open Access Transmission

In the NOPR, the Commission proposed to define who is eligible to receive service under a non-discriminatory open access tariff as follows:

A non-discriminatory open-access tariff must be available to any entity that can request transmission services under section 211.[281]

The Commission further explained that "[u]nder section 211, any electric utility, Federal power marketing agency, or any other person generating electric energy for sale tot resale may request transmission services under section 211."[282]

PSNM believes that the NOPR properly defined customer eligibility. NIEP, on the other hand. believes that the posed definition is too limited. It argues that the Commission should require public utilities to make transmission service available to all entities engaged in

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[281] *FERC Statutes and Regulations P* 32,514 at p. 33,083 (footnote omitted)

[282] *Id.* at p. 33,083 n.195.

wholesale purchases or sales of power, not just to those "generating" power. Utility Working Group requests that the Commission **[31,688]** clarify that eligibility is dependent not only on being the type of entity set forth in section 211, but on meeting the requirements of section 212(h) (Prohibition on Mandatory Retail Wheeling and Sham Wholesale Transactions) as well.[283]

We also received several comments related to the applicability of the rule to foreign entities. Canada states that the requirements for comparability and reciprocity should be implemented in a flexible masher to permit Canadian utilities to have fair and competitive access in the U.S. electricity market. Maritime requests that the Commission require Canadian utilities who wish to participate in the U.S. market to offer other utilities the same privileges they receive in the United States. Southwestern argues that transmission to a foreign country is in interstate commerce and that a utility should therefore accommodate this type of transmission request under its open access tariff. El Paso argues that the Commission does not have the authority to condition access to foreign countries, but states that if the Commission nevertheless exercises such authority it should do so on a case-by-case basis, Destec asserts that the posturing of Ontario Hydro before U.S. regulators pleading for open access and non-discriminatory transmission treatment – even for extra-territorial entities, should be met with a strong reply that such provisions should also be afforded transmission dependent entities on the Canadian side of the border. Ontario

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[283] Section 212(h) (Prohibition on Mandatory Retail Wheeling and Sham Wholesale Transactions).

Hydro's aggressive pursuit of U.S. market opportunities while simultaneously blocking competitors through the control of their transmission assets can not be ignored. Commission Conclusion.

In the Final Rule pro forms tariff the Commission has modified the definition of "eligible customer" to address concerns that in some respects the NOPR definition was too limited and in other respects it was too broad. This includes amended language to clarify that any entity engaged in wholesale purchases or sales of energy, not just those "generating" electric power, is eligible. It also includes clarification that entities that would violate section gig(h) of the FPA (prohibition on Commission-mandated wheeling directly to an ultimate consumer and sham wholesale transactions) are not eligible. The language also has been modified to provide that foreign entities that otherwise meet the eligibility criteria may obtain transmission services. Further, it has been modified to provide for service to retail customers in circumstances that do not violate FPA section 212(h).[284]

Persons that would be eligible section 211 applicants also would be eligible under the open access tariffs. Section 211 applicants may be any electric utility, Federal power marketing agency, or any other person generating electric energy for sale for resale.

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[284]We emphasize that any transmission customer must follow prudent utility practices so to assure reliability.

Section 3(22) of the FPA. as amended by the Energy Policy Act, defines "electric utility" co mean any person or State agency (including any municipality) which sells electric energy; such term includes the 'Tennessee Valley Authority. but does not include any Federal power marketing agency. Thus, as we have previously noted, municipal utilities are electric utilities simply by the terms of the statute.[285] In addition, we have also found that cooperatives and marketers are electric utilities as defined in the FPA.[286] Other entities that fall within the definition include IOUs, IPPs, APPS, and QFs that sell electric energy.

We do not believe that entities that engage solely in brokering should be eligible. Such brokers do not take title to electricity and therefore do not engage in the sale of electric energy; nor do they generate electric energy for sale for resale.[287]

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[285]New Reporting Requirement Implementing Section 213(b) of the Federal Power Act Supporting Expanded Regulatory Responsibility Under the Energy Policy Act of 1992, and conforming and Other Changes to Form No. FERC-714. Order No. 558-A, 65 FERC ¶61,324 at p. 62.451 n. 12 (1993).

[286]Order No. 558. *FERC Statutes and Regulations* ¶30,980 at p. 30,895-96, reh'g denied. 65 FERC ¶61,324 (1993) (cooperatives are electric utilities): *AES Power, Inc.*, 69 FERC ¶61,345 at p. 62.297 (1995) (power marketer is an electric utility, i.e., a person "which sels electric energy").

[287]*See, e.g., Citizens Energy Corporation*, 35 FERC ¶61,198 at p. 61.452-53 (1986).

[31,689]

Although such brokers are not eligible under the tariffs, they will be able to arrange deals because they will have access to the OASIS of all public utilities and will be able to solicit information from the relevant transmission service providers under the terms of the applicable tariffs.

We clarify that foreign entities that otherwise meet the eligibility criteria must be eligible to receive service under the non-discriminatory open access transmission tariffs.[288] We are making this determination pursuant to our authority under section 206 of the FPA to remedy undue discrimination. As we explained in the NOPR, market power through the control of transmission can be used discriminatorily to block competition. Customers in the United States should not be denied access to cheaper supplies of electric energy, whether such electric energy is from a domestic source or a foreign source. By making non-discriminatory access available to foreign entities that otherwise meet the eligibility criteria: we are assuring that customers in the United States have access to as many potential suppliers as possible. This should result in increased competition and lead to customers paying the lowest possible prices for their electric energy needs. To the extent that such an entity obtains access, however, we emphasize that it would be subject to all of the terms and conditions of the applicable open access tariff, including the requirement that it provide reciprocal service.

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[288]In making this determination, we are not deciding whether these entities are eligible entities under section 211(a) of the FPA.

Finally, we have reconsidered our NOPR position that would have limited eligibility to wholesale transmission customers. As we explained in the NOPR. the Commission's jurisdiction, extends to all unbundled transmission, in interstate commerce by public utilities. It is irrelevant to the Commission's jurisdiction whether the customer receiving the un-bundled transmission service in interstate commerce is a wholesale or retail customer. Thus, if a public utility voluntarily offers unbundled retail access interstate commerce or a state retail access program results in unbundled retail access in interstate commerce by a public utility, the affected retail customer must obtain its unbundled transmission service under a non-discriminatory transmission tariff on file with the Commission. Though the Commission may approve a separate retail transmission tariff when some variation is necessary or appropriate to meet local concerns,[289] we generally see no reason why retail transmission tariffs necessarily must be different from wholesale transmission tariffs. For that reason, we anticipate that in .many circumstances the same open access tariff that serves wholesale customers will be equally appropriate for retail transmission customers. Therefore, unless the Commission has specifically permitted a separate retail tariff, eligible customers under the Final Rule pro forma

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[289]See Section IV.I.

tariff must include unbundled retail customers,[290] We discuss this further in Section IV.I.

While the rates, terms, and conditions of all unbundled transmission service will be subject to a Commission-authorized tariff, we will, in appropriate circumstances, give deference to state recommendations regarding rates, terms, and conditions for retail transmission service or regarding the proper transmission cost allocation to be used between retail and wholesale customers when state recommendations are consistent with our open access policies. This is also discussed further in Section IV.I.

Moreover, we are mindful of the fact that we are precluded under section 212(h) from ordering or conditioning an order on a requirement to provide wheeling directly to an ultimate consumer or sham wholesale wheeling. We therefore clarify that our decision to eliminate the wholesale customer eligibility requirement does not constitute a requirement that a utility provide retail transmission service. Rather, we make clear that if a utility chooses, or a state lawfully requires, unbundled retail transmission service, **[31,690]** such service should occur under this tariff unless we specifically approve other terms.

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[290]The Commission has no authority to order retail transmission directly to an ultimate consumer or to order "sham" wholesale transmission, See FPA section 212(h). However. if such access occurs voluntarily or as a result of a state program, the rates, terms, and conditions of the access are within our exclusive jurisdiction if the service is provided by a public utility.

2. Service That Must be Provided by Transmission Provider

In the NOPR, the Commission proposed that a public utility must offer to provide any point-to-point or network transmission service whether or not the utility provides itself that service:

The Commission therefore proposes that all public utilities must offer both firm and non-firm point-to-point transmission service and firm network transmission service on a nondiscriminatory open access basis in accord with the proposed rule and the attached appendix tariffs. The Commission believes that a utility's tariff must offer in provide any point-to-point transmission service and network transmission service that customers need, even though the utility may not provide itself the specific service requested.[291]

EGA and SMUD agree that a transmission owner should offer any transmission service it is able to provide, even if it does not use the service itself:

Public Generating Pool, an association of consumer-owned electric utilities, appears concerned that the Commission may interpret comparability broadly to require a utility to offer the same service provided by another utility or to offer service generally available in a region. Thus, it recommends that a third party seeking more service than a utility provides itself be required to resort to the section 211 process.

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[291]FERC Statutes and Regulations ¶32,514 at p.33,079

Commission Conclusion

Initially, we note that, with the possible exception of small utilities (which may qualify for a waiver, see infra), we have seen no evidence that public utilities are incapable of reasonably providing the services required in the Final Rule pro forma tariff. Nor have we seen evidence that utilities able to provide these services to themselves are choosing to forego such services. In short, we are not convinced that there is an appreciable difference, if any, among the services required in the pro forma tariff, the services utilities are able to provide, and the services they actually provide themselves.

To the extent these services do differ, however, we explicitly adopt the proposal set forth in the NOPR. Thus, a public utility must offer transmission services that it is reasonably capable of providing, not just those services that it is currently providing to itself or others. Because a public utility that is reasonably capable of providing transmission services may provide itself such services at any time it finds those services desirable, it is irrelevant that it may not be using or providing that service today. Moreover. a public utility must offer these transmission services whether or not other utilities may be able to offer the same services and whether or not such services are generally available in the region (waiver of these requirements for .small utilities is discussed in Section IV.K.2.).[292] However, if a customer seeks a customized service not offered in an open access

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[292]Requirements for ancillary services are discussed in Section IV.D.

tariff, a customer may. barring successful negotiation for such service, file a section 211 application.

3. Who Must Provide Non-Discriminatory Open Access Transmission

In the NOPR, the Commission proposed to require all "public utilities" owning and/or controlling facilities used for transmitting electric energy in interstate commerce to file open access transmission tariffs.[293] We explained that we could not require all "transmitting utilities" to file open access tariffs under sections 205 and 206 because we do not have jurisdiction over non-public utilities under these sections.

Several commenters argue that the open access requirement must be applied to non-jurisdictional utilities that own interstate transmission facilities.[294] Power Marketing Association recognizes that this raises difficult legal issues and suggests that the Commission support legislation to expand the Commission's authority over non-jurisdictional utilities. Minnesota P&L argues that ir the requirement is not applied to all entities that own transmission, jurisdictional and **[31,691]** non-jurisdictional entities owning joint transmission facilities will be competitively disadvantaged due to unequal pricing. Union Electric argues that unless the requirement is extended to the 56 non-jurisdictional entities operating control areas, discrimination in the wholesale power markets will increase.

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[293] *FERC Statutes and Regulations* ¶32,514 at p. 33,049.

[294] *E.g.*, Minnesota P&L, Power Marketing Association.

A number of municipal commenters assert that the NOPR overlooks transmission assets jointly owned by jurisdictional and non-jurisdictional utilities.[295] They argue that agreements regarding use of these assets often contain provisions prohibiting third-party power transfers. They further argue that such provisions should be nullified, and the joint owners should be required to develop equitable methodologies to allocate wheeling revenues among themselves.

Several cooperatives urge the Commission to clarify that contracts among their constituent cooperatives are not subject to any unbundling of existing contracts.

Commission Conclusion

Our authority under sections 205 and 206 of the FPA permits us to require only public utilities to file open access tariffs as a remedy for. undue discrimination. We have no authority under those sections of the FPA to require non-public utilities to file tariffs with the Commission.

However, we are concerned that if nonpublic utilities do not provide access, there will remain a patchwork of "open" and "closed" transmission systems and the potential for distortions in wholesale bulk power markets. We believe that certain mechanisms exist that will help to alleviate these problems.

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[295]E.g., Springfield.

First, as we explained in the NOPR, broad application of section 211 will provide wider access to bulk power markets.[296] Under section 211, eligible entities may seek transmission service from "transmitting utilities," which section 3(23) of the FPA defines as "any electric utility, qualifying cogeneration facility, qualifying small power production facility, or Federal power marketing agency which owns or operates electric power transmission facilities which are used for the sale of electric energy at wholesale." We believe that section 211 provides us with authority to require the same quality of transmission service as sections 205 and 206, though the procedural path is more cumbersome. Thus, section 211 provides access to transmission systems owned or operated by non-public utilities.[297]

Second, as we explained in the NOPR, our reciprocity requirement is designed to provide the widest possible use of the nationwide transmission grid:

The purpose of this provision is to ensure that a public utility offering transmission access to others can obtain similar service from its transmission customers. It is important that public utilities that are required to have on file tariffs be able to obtain service from transmitting utilities that are not public

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[296] *FERC Statutes and Regulations* ¶32,514 at p. 33,050 and 33,092-93.

[297] As discussed in the NOPR, sections 211 and 212 require that applicants specify only fates, terms, and conditions of service, not specify transactions. Thus, applicants can file requests for tariffs to accommodate future currently unspecified transactions, similar to the open access tariffs required by this Rule.

utilities, such as municipal power authorities or the federal power marketing administrations that receive transmission service under a public utility's tariff.[298]

Finally, again as we explained in the NOPR, the formation of RTGs should speed the development of competitive markets and involve more non-public utilities in the provision of non-discriminatory open access transmission.[299] In approving RTGs, our policy has been to require all members, whether or not they are public utilities, to offer comparable transmission services at least to other members.

We recognize that these solutions are not perfect. However, given the difficulties inherent in the statutory scheme, we believe they will go a long way toward effectuating transmission access by nonpublic utilities,

One further issue involving non-public utilities concerns jointly owned transmission facilities. We will not allow public utilities that jointly own interstate transmission **[31,692]** facilities with non-jurisdictional entities to escape the requirements of open access. We will require each public utility that owns interstate transmission facilities jointly with a non-jurisdictional entity to offer service over its share of the joint facilities, even if the joint ownership contract prohibits service to third parties. we urge such public utilities to seek mutually agreeable revisions to their agreements to permit

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[298] *FERC Statutes and Regulations* ¶32,514 at p. 33,089.

[299] *Id.* at p. 33,095.

third-party access over all. or at least their share, of the facilities. For those joint ownership arrangements that include restrictions on the usage of jointly owned transmission facilities by third parties, we will require the public utilities, in a section 206 compliance filing. to file with the Commission, by December 31, 1996, a proposed revision (mutually agreeable or unilateral) to its contract with the non-jurisdictional owner(s). This revision must be designed at a minimum to permit third parties to use the public utility's share of the joint facilities in accordance with this Rule and must provide for any needed cost allocation procedures between the public utility and the non-jurisdictional owner(s).

4. Reservation of Transmission Capacity by Transmission Customers

In the NOPR, the Commission set forth the information that a requester of transmission service would have to submit with a service request. We recognized that there may have to be a limit, for competitive reasons, on the information required, but also recognized the need to assure that no customer would reserve scarce capacity and then hold it without using it.[300] To avoid forcing transmission customers to reveal unnecessary details of their purchase or sales transactions, the Commission discussed several less restrictive options: (1) Allow the transmission provider to use or sell the capacity while it is unused, (2) have a pool that clears the short-term market, and (3) require the customer to begin using the capacity within some specified period or lose its

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[300] *Id.* at p. 33,090.

reservation rights. The Commission requested comments on these and other possible approaches.

Unused or Unneeded Transmission Capacity

Many commenters recommend a use-it-or-lose-it rule (i.e., a transmission customer must use its reserved transmission capacity or lose its rights to that capacity).[301] Several commenters also recommend a number of restrictions on capacity reservations to reduce incentives to hoard or to cherry-pick (request to reserve firm capacity only during peak hours of peak seasons) existing transmission capacity. These include: (I) Allow requesters to reserve a place in the queue with a right o[first refusal over later competing requests; (2) impost a take-or-pay charge on reservations and deny reservation holders the right to revenue sharing if they do not schedule or assign their rights; (3) limit the time period for reservations; (4) limit how far in advance reservations may be made for both non-firm and firm services: (5) maintain a price cap on the resale of transmission; (6) require multi-year reservations to be for sequential periods; and (7) require a nonrefundable fee for advance reservations of service.[302] Southwestern suggests that transmission tariffs include a provision that prevents transmission customers and the

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[301] *E.g.*, Consumers Power, Northern States Power, PacifiCorp, Oklahnma G&E, Allegheny Power, ELCON, Public Service Co of CO.

[302] *E.g.*, Northern States Power, VEPCO, Utilities For Improved Transition, PacifiCorp, Arizona Public Service, Dairyland, Montaup, Illinois Power, South Carolina E&G, Florida Power Corp. KU.

transmission provider from reserving and tying up firm transmission capacity for speculative wholesale actions.[303]

On the other hand, PSNM believes that a use-it-or-lose-it approach is inappropriate because any prudent utility that has reserved capacity would seek to sell the service it is not using so as to recover some portion of its fixed costs. Wisconsin P&L argues that a use-it-or-lose-it approach would not work, would be difficult to administer, and may be anticompetitive.[304] Central Illinois Public Service asserts that a reservation holder has little incentive to hoard capacity because other customers can use the capacity on a non-firm basis during times when a reservation **[31,693]** holder does not schedule power. It warns that giving the transmission operator the ability to schedule unused capacity may result in undue influence and the exercise of market power. CA Energy Cpm maintains that, while reassignment would help prevent hoarding, it would not assure efficient use of the full transmission network,

Use of Pooling Arrangements To Prevent Improper Reservations

Allegheny Power contends that a pooling arrangement could provide an incentive to hoarders to release capacity during a shortage. It suggests that capacity could be auctioned within a pool pt available capacity. However, it acknowledges

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[303]See also NRECA.

[304]Wisconsin P&L notes, however, that a possible exception exists where a user could block the efficient transfer of power and then market its own power at a premium price.

that an auction would be tantamount to allowing the network owner to sell transmission service at unregulated rates.

PacifiCorp does not believe that a pooling arrangement would prevent capacity hoarding unless nonsequential reservations are prohibited ELCON contends that a use-it-or-lose-it rule would be fairer and more effective than pooling.

Commission Conclusion

Upon further consideration, we conclude that firm transmission customers, including network customers, should not lose their rights to firm capacity simply because they do not use that capacity for certain periods of time. Firm transmission customers that have reserved capacity and paid a reservation charge generally do not use the entire amount of reserved capacity at all times. This does not mean, however, that they must permanently return the unused amount to the utility. In the absence of evidence of hoarding or other anticompetitive practices, we will not limit the amount of transmission capacity that a customer may reserve. Firm transmission customers are in the best position to know the levels of electric energy they will be transmitting and the level of flexibility they need in carrying out their transmission activities. Indeed, when they are not using their reserved capacity, firm transmission customers remain obligated to pay the utility a reservation charge that covers all of the utility's fixed costs associated with the reserved capacity.[305]

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[305]A reservation charge would assure that the utility fully recovers its fixed costs associated with the transmission customer's reserved transmission capacity.

Moreover, the possibility that a customer will reserve capacity and then hold it without using or reassigning it is mitigated because the utility is free to schedule and sell any unscheduled firm point-to-point transmission capacity on a non-firm basis to any entity eligible to receive such service under the utility's tariff. We also note that it is in the economic self interest of reservation holders to make available unused capacity to the market.[306]

We recognize that situations could arise in which a customer unlawfully withholds capacity. That is, a transmission customer could retain capacity in a way that could have an anticompetitive effect. For example, a transmission customer may serve certain capacity simply to prevent everyone else From using it and to make its own generation the only alternative available to the market. However. as described above, we believe that the incentives are such that parties are more likely to release unneeded capacity and that a generic remedy is therefore unnecessary. Any substantial allegations that indicate that a transmission customer is withholding scarce capacity in a way that has an anticompetitive effect would be addressed under section 206. If we round such allegations to be true, we could order the customer to return the capacity reservation right to the transmission operator. This approach should allay concerns that a customer may reserve scarce capacity and nat use it, without forcing customers to demonstrate need or to reveal details of individual transactions.

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[306]See Section IV.C.6.

5. Reservation of Transmission Capacity for Future Use by Utility Comments

EEI and many IOUs argue that native load and network transmission customers should have first priority to existing capacity for their reasonably forecasted load requirements because that capacity was constructed to provide service to them and was paid for by them.[307] EEI contends that such priority ensures **[31,694]** equity and comparability based on past and future cost responsibility for the system. Similarly, Florida Power Corp and PECO contend that third-party customers should not be allowed to use transmission capacity that native load customers would grow into within a reasonable planning horizon.

Other commenters disagree, asserting that available transmission capacity must be determined in the same manner for all customers and that utilities should not be permitted to reserve capacity for their own uses.[308] NIEP argues that utilities should not be permitted to lock up available transmission capacity over valuable transmission paths and then require transmission requesters to pay for the cost of incremental transmission upgrades. This would let the utility avoid incremental transmission charges on its system.

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[307] *E.g.*, NYPP, Public Service E&G, Sierra Pacific Power, Ohio Edison, Sierra Pacific Power asserts that a utility should be permitted to retain capacity for native load use over the pertinent planning period. El Paso adds that the Commission should allow utilities the opportunity to reserve capacity for anticipated uses that, although not firm, are necessary to maintain reliability.

[308] *E.g.*, NIEP, CCEM, Conservation Law Foundation.

Oklahoma G&E argues that existing available transmission capacity should be made available until it is needed for native load growth. Utilicorp states that transmission owners should not be permitted to set aside capacity for sales or purchases of economy energy. CCEM argues that the centerpiece of comparability is that ail transmission customers, including the merchant operations of the transmission owner, take service from available capacity pursuant to the same tariffs. CCEM .adds that allowing utilities to reserve capacity based on forecasted retail and network loads creates an incentive for them to over-forecast their load to the detriment of all others. NRECA suggests that the need to maintain reliability should not perpetuate transmission providers' preferential treatment of their own transactions. It also recommends that, during periods when facilities are constrained, access be allocated based on a combination of past actual use and planned future use.

Commission Conclusion

We conclude that public utilities may reserve existing transmission capacity needed for native load growth and network transmission customer load growth reasonably forecasted within the utility's current planning horizon. However, any capacity that a public utility reserves for future growth, but is not currently needed, must be posted on the OASIS and made available to others through the capacity reassignment requirements, until such time as it is actually needed and used.

In response to arguments raised by several commenters that existing requirements customers should have future right to existing capacity beyond the terms of their contracts

because of their historical use, as discussed previously, we believe existing customers should have a right of first refusal to capacity they previously used. if they are willing to match the rate offered by another potential customer, up to the transmission provider's maximum filed transmission rate at that time, and to accept a contract term at least as long as that offered by another potential customer.[309]

6. Capacity Reassignment

In the NOPR, the Commission proposed that a tariff must explicitly permit reassignment of firm service entitlements.[310] We explained thai reassignment of capacity rights could have a number of benefits: (1) Helping transmission users manage financial risk. (2) reducing transmission providers' market power by enabling transmission customers to compete with them, and (3) improving capacity allocation when capacity is constrained and some market participants value capacity more than current capacity holders. We requested comments on whether the current price cap on resale should be modified or eliminated and whether the transmission services described in the NOPR are suitable for reassignment.

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[309]See Section IV.A.5.

[310]*FERC Statutes and Regulations* ¶32,514 at p. 33,088.

General

Many commenters favor capacity reassignment and the development of secondary markets.[311] However, WP&L notes that reassignments should not be permitted over constrained interfaces if the **[31,695]** source or destination of power changes, and LA DWP opposes unrestricted reassignment because it could cause tax-exempt financing problems for many public power utilities.

Many IOUs argue that the same terms and conditions of service applied to IOUs should be applied to resellers of transmission services?[312] Arizona Public Service. however, asserts that all unused transmission rights should not be assignable, but should be made available to others in a manner consistent with the contract supporting the rights, it argues that a network user experiencing an off-system network shutdown should be required during the outage to make available to others the path from the point that the power enters the system to its load. It also contends that firm transmission customers should be required to post their unused rights on an EBB or RIN.

Several commenters oppose mandatory reassignment of firm capacity rights.[313] NEPCO declares that if a customer

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[311]*E.g.*, PacifiCorp, DOJ, NIEP, ELCON. United Illuminating, DOD, WP&L, FTC, OK Com and FL Com favor reassignment of capacity that reliability not be affected.

[312]*E.g.*, Northern States Power.

[313]*E.g.*, NEPCO, Nebraska Public Power District.

is willing to pay for its reserved capacity, it should not be forced to reassign unused capacity. Nebraska Public Power District believes that mandatory reassignment could cause problems for publicly-owned utilities. It further asserts that in the gas industry the Commission did not allow the unregulated reassignment regime it proposes for the electric industry.

SoCal Edison argues that when a transmission customer resells transmission capacity, it should not be released from its contractual obligation to the transmission provider. It notes that under traditional contract law, a party to a contract cannot escape its obligations by delegating them to another.

Price Caps

Most commenters addressing this issue support retaining the existing price capon reassignments or resales.[314] Generally, these commenters believe that the price cap is necessary to prevent customers from speculating or hoarding capacity in anticipation of its value increasing. Public Service Co of CO believes that allowing assignments of capacity at prices greater than cost could prevent a transmission provider from offering firm capacity for legitimate long-term transactions. TDU Systems states that a cap should remain

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[314] *E.g.*, NRECA, Montana Power, PacifiCorp. NYSEG, PA Corn, Idaho. Public Service Co of CO, FPC, Entergny, TDU Systems, Duke, Cajun, CVPSC, Oglethorpe, Minnesota DPS. FL Com argues that the price of reassignment should be capped at the contract selling price. WP&L argues that the price cap should be raised to the maximum rate allowed in the tariff under which the user purchased the original service.

until the secondary market in the relevant geographic market has been shown to be competitive. PA Corn states that turning available capacity into a spot market would tie up capacity that might otherwise be used on a day-to-day basis and for emergencies. Still other commenters argue that customers should not be allowed to sell the capacity for more than the transmitting utility could charge.[315] Allegheny argues that any rule that allows resale of transmission capacity at a higher price than the transmission provider can achieve is "patently illogical and probably illegal." Several utilities, including Allegheny and CSW. contend that if resellers can market transmission services at market rates, then transmission owners must be given the same opportunity.

Duquesne and United Illuminating argue that the price cap should be modified so that third parties are allowed to resell capacity at the higher of embedded costs or opportunity costs.[316] Duquesne notes that such a provision would be comparable to the option transmitting utilities now have and would be economically effi-dent because it would encourage the firm capacity owner with the lowest opportunity cost to resell its capacity.

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A few commenters argue that the price cap should be eliminated.[317] IL Corn claims that capacity will be made available to the entity that values it most and that an uncapped

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[315]See also Minnesota DPS.

[316]See also Midwest Commission, SMUD, CCEM.

[317]*E.g.*, IL Com, NEPCO, Consumers, American Wind.

resale market cannot lead to more market power because an efficient secondary market cannot be monopolized. Con Ed agrees that if the secondary market is competitive, all entities should be allowed to sell at market-based rates.[318] CT DPUC argues that there should not be a price cap: instead, it would prefer that those holding transmission rights not be allowed to withhold use of any portion of their reserved transmission capacity in the actual moment-by-moment operation of the grid.

Creditworthiness Standards

Of those commenting on the appropriate creditworthiness standards for replacement customers (assignees), all favor allowing the transmission provider to use reasonable credit procedures to assure that the replacement customer is financially sound.[319] NYSEG suggests that. at a minimum, the same creditworthiness criteria should be applied to the replacement customer as are applied to the original customer. Oglethorpe recommends that the assignee be required to commit to comply with all customer obligations and to pay for any additional costs resulting from the assignment.

Liability for Payment

Commenters split on whether the original customer or the replacement customer should be liable to the transmitting

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[318]If the market is not competitive, however, Con Ed maintains that the cap should be retained for all entities.

[319]*E.g.*, PacifiCorp, NYSEG, Oglethorpe.

utility for payment for the service. One group of commenters believes that the original customer should remain liable for all costs and for the performance of all obligations.[320] Another group of commenters believes that the original customer should be relieved of financial responsibility, at least under certain circumstances.[321] For example. NYSEG asserts that the original customer should be relieved of its obligations upon the execution of a new service agreement between the new customer and the provider. TDU Systems contends that the original customer should be relieved of future liability where the replacement customer meets the transmission provider's creditworthiness standards. Entergy argues that the original customer should, remain liable until all obligations are fulfilled.

Commission Conclusion

After reviewing the comments, we conclude that a. public utility's tariff must explicitly permit the voluntary reassignment of all or part of a holder's firm transmission

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[320]*E.g.*, Oglethorpe, NSP.

[321]*E.g.*, NYSEG, Entergy, TDU Systems, Trulock, American Wind.

capacity rights[322] to any eligible customer.[323] Reassignment may be on a temporary or permanent basis, and must be subject to the condition and requirements discussed below.

Allowing holders of firm transmission capacity rights to reassign capacity will: (1) Help them manage the financial risks associated with their long-term transmission commitments, (2) reduce the market power of transmission providers by enabling customers to compete, and (3) foster efficient capacity allocation. We offer below a number of clarifications and further explanations in response to concerns raised by commenters.

(1) Reassignable Transmission Services

We conclude that point-to-point transmission service, because it sets forth clearly defined capacity rights, should be reassignable. As for network transmission service, we conclude that there are no specific capacity rights associated with such service, and thus. network transmission service is not reassignable.

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[322]The transmission provider has the same rights as any other potential assignee to obtain capacity that is posted on an OASIS or to negotiate with the assignor for any capacity the assignor seeks to assign.

[323]The public utility's tariff shall not preclude an assignor from including a right of recall in its agreement with an assignee.

(2) Terms and Conditions of Reassignments

a. General

In effecting a reassignment, the assignor does not have to return its capacity entitlement to the original transmission **[31,697]** provider, but may deal directly with an assignee without involvement of the transmission provider. However, an assignee must meet the eligibility standard established by this Rule and must comply with the reliability criteria of the original transmission provider. Any such transaction must be posted on the transmission provider's OASIS within a reasonable time after its effective date. Alternatively, the assignor may, if it wishes, request the transmission provider to effect a reassignment on its behalf.[324] In such a situation, the transmission provider must immediately post the available capacity on its OASIS. The transmission provider must assure that any revenues associated with the reassignment are credited to the assignor.[325]

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[324]The assignor may also request the transmission provider to provide the billing and payment services for the reassignment. The parties would negotiate terms for such an arrangement, including a fee for the transmission provider. If an assignor is a public utility, it will have to have on file with the Commission a rate schedule governing reassigned capacity.

[325]Any expenses that the public utility incurs in carrying out the capacity assignment program would simply be included in its cost of service.

b. Contractual Obligations

Assignors and assignees may contract directly with each other, but the assignor will remain obligated to the transmission provider, This obligation extends to any penalties or other charges incurred by the assignee in its use of the reassigned capacity, The assignee will be liable solely to the assignor, and should it not meet its obligations, the assignor may cancel the assignment under their contract.

If the transmission provider and the original customer mutually agree, we will permit alternatives to the above approach. For example, the transmission provider could agree to relieve the original customer of payment liability for the term of the reassignment and permit the assignee to pay the provider directly.

In the case of a permanent reassignment. the transmission provider should not unreasonably refuse to release the assignor from liability if the assignee meets the transmission provider's creditworthiness requirements as set forth in its tariff and agrees to pay the price the assignor is obligated to pay the transmission provider.

c. Price Cap

We conclude that the rate for any capacity reassignment must be capped by the highest of: (1) The original transmission rate charged to the purchaser signor), (2) the transmission provider's maximum stated firm transmission rate in effect at the time of the reassignment, or (3) the assignor's own opportunity costs capped at the cost of expansion (Price Cap). We remain convinced that we cannot

lift the Price Cap and permit reassignments at market-based rates. Based upon the information available in this proceeding, we are unable to determine that the market for reassigned capacity is sufficiently competitive so that assignors will not be able to exert market power. Thus, we will not permit an assignor to reassign capacity at a rate in excess of the Price Cap. Assignees must agree, in contracting with the assignor, that the firm transmission capacity they will use is subject to the Price Cap.

7. Information Provided to Transmission Customers Comments

Many commenters argue that in an open access, competitive environment, confidential and proprietary information should not be made publicly available through a RIN.[326]

Several utilities assert that the existing reporting requirements are sufficient to support the comparability requirements of the proposed rule, with some modifications.[327] They note that the Commission's audit authority and complaint process will help enforce comparability requirements.[328] Central Illinois Public Service

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[326]Similar arguments with respect to the information that public utility must provide to the Commission in standard reports (*e.g.*, Form No. 1) are addressed later in this Final Rule.

[327]*E.g.*, PacifiCorp, NYSEG, NSP.

[328]See also PA Com.

states that, with the availability of pricing and transaction information through the RIN, no further reporting requirements are necessary. IL Com states that additional reporting should be required only if clear evidence emerges of discriminatory use of the transmission system. Dominion Resources adds that users have **[31,698]** no need for utility planning information and data on generator status and that disclosure of such information would place owners at a competitive disadvantage. VEPCO opposes the disclosure of any commercially sensitive information to marketers, including the utility's power marketing employees.

On the other hand, several commenters argue that the information submitted by public utilities may not be adequate. For example, APPA argues that the Commission should scrutinize closely cost functionalization by utilities to assure that plant in service is properly booked. Others recommend that the Commission put in place a monthly pass-through of transmission-related operating income for all classes of customers receiving firm transmission service, rather than rely on the current practice of reducing test year cost of service by revenues booked to Accounts 456 and 447. Industrial Energy Applications recommends that utilities be required to file quarterly reports with the Commission that detail the transmission services and the pricing of their off-system power supply transactions, as an incentive to comply with the Commission's rule. Commission Conclusion

We conclude that all necessary transmission information, as detailed in the OASIS final rule, must be posted on an OASIS. With respect to generation information, we will require, consistent with the OASIS final rule, that information needed to verify opportunity/redispatch costs be

provided, on request, to the transmission customer charged, We will not require this information, or any other generation information,[329] to be posted on an OASIS.[330]

[31,698]

8. Consequences of Functional Unbundling

a. Distribution Function

The NOPR proposed functional unbundling of wholesale generation and wholesale transmission so that the public utility as a wholesale seller could not gain an undue advantage from its transmission ownership. We did not propose to further unbundle the retail transmission and distribution functions from the wholesale transmission function.

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[329]The prices of some ancillary services, which are posted on the OASIS, are based on generation tusks, however.

[330]Because the Commission establishes many generation and all transmission rates on a cost basis, the Commission also will continue to sell the information that it collects in Form No. 1 and other standard forms from public utilities to assure that the rates arc just and reasonable. As we explain later in this Final Rule. the information provided in those forms is public information that is available to any transmission customer. However, because of the competitive changes occurring in the electric industry, we recognize that there may be a need to reexamine the information we collect from public utilities through the Form No. 1.

Comments

A number of commenters assert that utilities should be required to unbundle -- either functionally or corporately -- the distribution function from the transmission function. ELCON argues that unbundling distribution would help delineate state and Federal jurisdiction, facilitate the establishment of transmission pricing, avoid cross-subsidization, and prepare for the customer choice (retail wheeling) programs that will be implemented by states in the future. It contends that functional distinctions between wholesale and retail service should be minimized.[331]

Other commenters, however, oppose establishing a separate distribution function. DOD asserts that the Commission can address any problems that arise by enforcing the terms of open access tariffs and that the Commission should not intrude into state ratemaking.[332]

Various state commissions question the workability and desirability of a functional test to determine the dividing line between retail transmission and local distribution.[333] CA Com recommends that, to avoid jurisdictional uncertainty surrounding functional unbundling, the Commission adopt a functional test for local distribution. Under this test, vertically

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[331]See also Environmental Action, Missouri Basin MPA, Texaco, EGA, AEC & SMEPA.

[332]See also TDU Systems, Public Service Co. of CO.

[333]*E.g.*, NARUC, AZ Com, CT DPUC, OK Com, FL Com, NC Com, NM Com.

integrated utilities that chose to unbundle **[31,699]** into separate operating companies, including a local distribution company that sells only at retail, could establish a workable bright line between state and federal authority without engaging in the arduous task of differentiating transmission from distribution.

Certain IOUs echo the jurisdictional concerns raised by the state commissions.[334] They believe that the unbundling of the distribution function would create significant jurisdictional problems. Pacificorp also argues that unbundling of the distribution function would create significant jurisdictional conflict with respect to cost allocation.

Commission Conclusion

We conclude that the additional step of functionally unbundling the distribution function from the transmission function is not necessary at this time to ensure non-discriminatory open access transmission. Our approach to assuring such open access has two broad requirements: (1) functional unbundling of transmission and generation (which includes separately stated rates for generation, transmission, and ancillary services, and a requirement that a transmission provider take service under its own tariff), except for bundled retail service and (2) an OASIS with standards of conduct. We believe that additional requirements are not needed now. We further address in Section IV.I the concerns raised regarding

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[334] *E.g.*, Com Ed, Citizens Utilities, PacifiCorp.

our proposed tests to distinguish transmission and local distribution.

b. Retail Transmission Service

The majority of commenters addressing this issue believe that unbundling retail service is unnecessary to establish a competitive market and to achieve non-discriminatory open access transmission.[335] For example, PSNM argues that the Commission is not as well situated as are state regulators to oversee and supervise local reliability issues for retail customers. Central Illinois Public Service argues that due to the nature of transmission facilities and operations, it is not possible for the transmission provider to discriminate between the provision of wholesale and retail firm service. Several IOUs further contend that because the Commission is specifically precluded from mandating retail wheeling and has no authority over bundled retail service, the Commission cannot require retail service to be provided.[336]

In contrast, some commenters argue that functional unbundling must apply to all transmission service in interstate commerce provided by public utilities, including the transmission component of bundled retail sales.[337] They believe that this is necessary to achieve comparability. For

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[335]*E.g.* Allegheny Power, PacifiCorp, MidAmerican, PECO, Public Service Co of CO, Com Ed, NARUC, NRRI, MN DPS, ND Com, FL Com.

[336]*E.g.*, Allegheny Power.

[337]*E.g.*, CCEM, ABATE.

example, CCEM asserts that if the distribution function is not unbundled, the result will be service under two separate arrangements -- an explicit wholesale transmission tariff filed at the Commission and an implicit retail transmission tariff governed by a state regulatory body. According to CCEM, failure to unbundle retail transmission will allow transmitting utilities to manipulate how they characterize and account for their own uses of transmission. ABATE contends that the Commission, for efficiency reasons, should encourage states to permit retail access. It asserts that the Commission must adopt a policy that signals to states how rates, terms, and conditions of retail service will be established; once a state sets such parameters, the Commission should review them.

Commission Conclusion

Although the unbundling of retail transmission and generation, as well as wholesale transmission and generation, would be helpful in achieving comparability, we do not believe it is necessary. In addition, it raises numerous difficult jurisdictional issues that we believe are more appropriately considered when the Commission reviews unbundled retail transmission tariffs that may come before us in the context of a state retail wheeling program. The Commission therefore reaffirms its decision to require the unbundling **[31,700]** only of wholesale transmission from generation.[338]

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[338]But see discussion of buy/sell transactions in Section IV.I.

c. Transmission Provider

1. Taking Service Under the Tariff

In the NOPR, we explained that a public utility must take transmission services for all of its new wholesale sales and purchases of energy under the same tariff of general applicability under which others take service.[339]

A number of commenters argue that utilities should be required to take all of the transmission for their own use under their tariff.[340] CCEM asserts that a transmission owner should have to schedule, at arm's length, its retail transmission uses and pay posted rates into a separate account; otherwise the capacity might be overforecast at no cost.

PECO requests that the Commission clarify that the requirement that a transmission provider take service under its own transmission tariffs does not apply to: (1) retail service, (2) existing wholesale contracts, and (3) pooling arrangements. UNITIL claims that the requirement for a transmission provider to take service under its own tariff and to post its own tariff rate should not apply to pool transactions where a single pool-wide rate is applied.

A number of IOUs contend that it is not necessary for the transmission provider to take service under the network

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[339]*FERC Statutes and Regulations* ¶32,514 at p. 33,080.

[340]*E.g.*, Michigan Systems, Cleveland, Municipal Energy Agency Nebraska, Missouri Basin MPA, TAPS, Wisconsin Municipals, LG&E, NIEP, CCEM.

tariff because both the transmission provider and the network customers cannot use the tariff to make off-system sales. LILCO states that it is appropriate to distinguish between a transmission owner's use of its transmission system to make: (1) wholesale bulk power sales; and (2) off-system purchases to serve its native load retail customers. LILCO contends that in the second situation it should not be required to take transmission service under its own open access tariffs.

EGA argues that transmission owners should be required to take transmission service under open access tariffs for both wholesale off-system sales and purchases. It maintains that, as retail competition increases, utilities will eventually have to take retail service under their own tariffs. Power Marketing Association believes that comparability can be achieved only if transmission service provided in connection with coordination transactions is unbundled and the transmission provider takes such transmission service under its tariff.

Consumers Power also claims that there is an inconsistency between the NOPR text, the tariffs, and the proposed regulatory language regarding whether the requirement for a utility to take service under its own tariff applies only to new wholesale transactions. Commission Conclusion

We conclude that public utilities must take all transmission services for wholesale sales under new requirements contracts and new coordination contracts under

the same tariff used by others (eligible customers).[341] For sales and purchases under existing bilateral economy energy coordination agreements, we will give an extension until December 31, 1996, for public utilities to take transmission service under the same tariff used by others.[342] As further discussed in Section IV.F., we will also give an extension of time to December 31, 1996, for certain existing power pooling and other multi-lateral coordination agreements to comply with this requirement. This will ensure that utilities live by their own rules for wholesale transactions and that we can achieve non-discriminatory open access transmission. In the case of a public utility buying or selling at wholesale, the **[31,701]** public utility must take service under the same tariff under which other wholesale sellers and buyers take service.

2. Accounting Treatment

In the NOPR, we did not address any accounting aspects of our proposed rule.

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[341]With the exception of certain contracts and agreements executed on or before 60 days after publication of the Final Rule in the Federal Register, the regulation we are adopting requires that public utilities take service under their open access tariff for wholesale sales or purchases of electric energy and unbundled retail sales of electric energy, effective on the date the public utility engages in such transactions.

[342]As discussed in Section IV.F., the Commission will not impose this requirement on existing bilateral non-economy coordination agreements, but persons may file complaints that such agreements need to be modified.

IOUs generally object to a requirement that they pay themselves for their use of the transmission system.[343] NEPCO claims that it is a general principle of accounting that an enterprise cannot recognize and record revenues to itself. NEPCO suggests that, to ensure that utilities' financial statements are not misleading, this aspect of functional unbundling can and should be accomplished through the ratemaking process, rather than by requiring utilities to actually charge themselves revenues for taking transmission services.[344]

Atlantic City Electric states that the added costs of properly administering and accounting for these transactions separately will increase prices to ultimate consumers. It contends that ensuring that operators do not give undue preference to transactions of the transmission provider makes it unnecessary for a utility to charge itself.

CSW argues that some of the provisions of the tariffs were specifically designed for third parties and do not make sense as applied to the transmission provider (e.g., signing service agreements and running credit checks).[345]

Most IOUs suggest that a revenue credit mechanism be used to account for a transmission provider's use of its system. Florida Power Corp states that revenue credits should be equal to the utility's posted rates for transmission service

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[343]*E.g.*, EEI, Con Ed, VEPCO.

[344]See also NEPCO.

[345]See also Florida Power Corp.

multiplied by the amount of capacity reserved and/or energy transmitted by the utility.

Otter Tail proposes a revenue credit that allocates revenues based on use under the tariff of the utility's transmission investment and credits these revenues against the firm load customers' accounts.

Duke asserts that the transmission provider should maintain records reflecting transmission for its own transactions under the tariff and develop appropriate revenue credits for transmission rates. It also believes that all firm users of the transmission system should receive credits for all non-firm uses.

Allegheny Power states that the crediting of non-firm revenues to network customers would have to be done on an after-the-fact basis when their loads would be known. However, it believes that revenue crediting should occur only if the firm service customer has retained the utility to remarket the customer's unused capacity.

Cajun proposes that all transmission revenues in excess of those implicitly included in the development of the transmission rates, including those that the utility has charged itself, be credited back to the network service transmission customers on a load ratio share basis. If transmission service rates are formula rates that are recalculated annually, Cajun proposes that excess transmission revenues be used to offset the recalculated revenue requirement. If the rates are not formula rates, Cajun states that an explicit tracker with monthly crediting to the network customer must be used.

To avoid cross-subsidization between affiliates and third parties, NRECA suggests that transmission revenues "paid" by a utility's generation function to its transmission function be credited back to the utility's nonaffiliated customers, and that any rate discounts extended to the generation function by the transmission function be filed with the Commission with a full explanation of why the discount was extended together with a showing that the discount was made available to all other similarly situated customers.

APPA contends that the Commission's current system of revenue crediting could give transmission owners an unfair competitive advantage by allowing them to use the revenue credit to subsidize the price at which they sell power. It argues that transmission owners should pay the actual price of transmission rather than booking a revenue credit as an offset to the cost of transmission service.

TAPS and Wisconsin Municipals argue that an essential element of true comparability **[31,702]** is the ongoing pass-through to network customers of a load ratio share of transmission revenues generated by third-party and the transmission provider's off-system uses of the transmission system.

Houston L&P suggests that the revenue crediting mechanism proposed in the NOPR could be established to recognize the utility's transmission service revenue and expenses in non-third-party wheeling transactions by reclassifying a portion of its revenue equal to the cost of transmission services provided to itself during such transactions. This mechanism would not reclassify expense accounts, but would distinguish that transmission portion of

the total transaction's revenue that was associated with covering the cost of transmission service, using the rates charged in similar third-party transactions.

PacifiCorp contends that the Commission should enforce the requirement that utilities account for revenues they pay themselves through the Commission's audit powers and through complaint proceedings. It specifically recommends that each transmitting utility be required to indicate, in its Form No. 1 under Account 456, the megawatts and revenues associated with its firm and non-firm off-system sales.[346]

MT Com states that the embedded costs that the Commission functionalizes for jurisdictional purposes should be carefully reconciled with plant balances used to calculate other costs of service.

CCEM wants each transmission provider to charge and book revenues into separate accounts for (1) service provided to itself and off-system sales and third-party sales under the tariffs, (2) impact study costs that the provider performs for itself or an affiliate, and (3) ancillary service revenues, net of out-of-pocket expenses the transmission owner provides itself or an affiliate.

Arizona Public Service recommends that any revenue crediting or booking be prospective only and that enforcement

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[346]If the utility is not required to file a Form No. 1, PacifiCorp states that it should be required to file similar information annually.

occur through the Commission's periodic audits and a utility's rate cases.

Many IOUs argue that there should be no obligation to credit non-firm transmission revenues to customers who are not using their firm capacity.[347] PacifiCorp contends that all non-firm revenues should be credited against total annual revenue requirements, resulting in lower rates to all customers. Wisconsin P&L maintains that non-firm sales revenue should be shared with all network customers.

Otter Tail argues that non-firm transactions between existing utilities to support and achieve real-time system optimization should be permitted without charge to the transmission owner. CSW asserts that no credits should be made for the non-firm secondary service under the point-to-point tariff and that off-system purchases for native load should not result in a revenue credit.

Southwestern suggests that the Commission not require the crediting of a transmission component associated with off-system purchases by the public utility. Southwestern argues that a credit would interfere with a utility's ability to buy the most economic energy for its native load customers. It also argues that requiring a credit is not comparable to what network customers pay. NEPCO points out that crediting transmission associated with purchases would require native load customers to pay the costs of the utility's purchasing off-system power while network customers do not have to pay a

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[347] *E.g.*, Consumers Power, Northern States Power, PacifiCorp, Allegheny Power.

separate point-to-point charge for their off-system purchases. Southwestern claims that the crediting requirement would double-charge the transmitting utility and its native load customers because a utility's off- system purchases directly relate to the load it serves, and that load already is reflected in the transmission rate calculation. Southwestern also claims that it is unclear from the NOPR whether the Commission considers sales from the renewal of existing wholesale requirements contracts as being subject to crediting. It argues that transmission related to these sales should not be subject to the crediting requirement because this is service to native load customers.

[31,703]

Brazos opposes imputing revenues associated with a utility's own use of its transmission system because this will artificially increase the cost of power and deny consumers the benefits of economy energy sales made at market-based prices. Commission Conclusion

While we used the word "accounting" in the NOPR, the real issue is assuring that utilities bear the costs associated with their own uses of the system in a manner comparable to how they charge others. Accordingly, this is a rate issue, not an accounting issue. However, we direct utilities to account for all uses of the transmission system and to demonstrate that all customers (including the transmission provider's native load) bear the cost responsibility associated with their respective uses.[348]

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[348]Additional guidance on this subject is in Section IV.G.4.g.(2)(a).

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[pp. 31,718 - 31,736]

[31,718]

b. Services that May Be Offered and Sold as a Package

The NOPR indicated that ancillary services must be offered separately from one another but did not indicate if the transmission provider may also offer a package of ancillary services.

Comments

Several commenters support giving customers the option either to purchase ancillary services as separate and distinct services or to purchase a package of services from the transmission provider.[394] Others, such as Tallahassee, recommend that utilities be prohibited from bundling the purchase of one service with another so that a transmission customer cannot **[31,719]** rely on the transmission provider for just one or a few of the ancillary services.

EEI and ELCON argue that the Commission should permit customers the option to request that transmission providers offer packages of selected ancillary services.[395] They and other commenters express a concern that

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[394]*E.g.*, Direct Service Industries, Mt. Hope Hydro, ELCON, PA Com.

[395]EEI Initial Comments at V-4; ELCON Initial Comments at p. 21.

efficiencies can be lost under a policy that precludes combining ancillary services.

Commission Conclusion

We conclude that a transmission provider must offer and price the individual ancillary services separately. It may not tie the purchase of one to the purchase of another.

However, we will allow a transmission provider to assemble packages of ancillary services (not bundled with basic transmission service) that can be offered at rates that are less than the total of individual charges for the services if purchased separately. It may also offer rate discounts on any ancillary service. If a rate discount is offered to the transmission owner itself or to an affiliate of the transmission owner, the same discount must be offered to non-affiliates, as well. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory. All discounts must be posted on the transmission provider's OASIS.

4. Reassignment of Ancillary Services

In the NOPR, the Commission noted that ancillary services may not be suitable for reassignment and requested comments on this issue.

Commenters express divided views on the reassignment issue. Some IOU commenters believe that, subject to technical limitations, ancillary services could be

reassigned.[396] Other commenters, including many IOUs, oppose reassignment because they believe it is impractical.[397] In particular, PacifiCorp claims that the customer-specific nature of generation-related ancillary services prevents such services from being reassigned.

TDU Systems argue that transmission customers that must pay for ancillary services they do not need should be able to resell them to someone else.[398] Mt. Hope Hydro claims that, if a bulk power transaction and the associated transmission service can be reassigned, it is reasonable that the ancillary services used to support the transaction also should be reassigned, particularly if the same facilities and contract path are used.[399]

Commission Conclusion

We conclude that transmission customers will be allowed to reassign ancillary services along with the reassignment of basic transmission service. The Commission believes that a policy of transmission capacity reassignment may not be possible unless the ancillary services used to support the transmission are also reassignable.

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[396]*E.g.*, WP&L, NYSEG.

[397]*E.g.*, Consumers, PacifiCorp, Carolina P&L, PSNM, Salt River, PA Com, TDU Systems.

[398]TDU Systems Initial Comments at p. 87.

[399]Mt. Hope Hydro Initial Comments at p. 17.

5. Pricing of Ancillary Services

In the NOPR, we asked for comments on ancillary service pricing and proposed specific ancillary services prices in the Stage One implementation rates. Many commenters commented on the Stage One rates. There is no Stage One in the Final Rule.

Many commenters state that ancillary services are difficult to price. They suggest diverse pricing approaches. IN Com notes that, because utilities and regulatory commissions have no experience with pricing unbundled ancillary services, the process needs to evolve but the goal should be to encourage market pricing in competitive markets. Air Liquide believes the best pricing policy should be negotiated bilateral agreements, provided market power is mitigated.

Other commenters express concern about how pricing proposed in the NOPR would affect the development and operation of competitive ancillary services markets. Industrial Energy Applications notes that low price caps on generation-related services, such as supplying losses, imbalance energy, operating reserve and backup power, which can be provided from many sources, inhibit competitive **[31,720]** market development. There is little incentive for other providers to invest in facilities to provide these services. Dayton P&L and others contend that the Commission should not require transmission providers to provide generation-based ancillary services at cost-based rates and then allow third parties to resell such services at market-based rates. PacifiCorp expresses concern that the NOPR's pricing proposal would be overly restrictive in the emerging competitive market for generation-related ancillary services.

Many commenters argue that cost-based price caps are appropriate for ancillary services if there are no alternative suppliers or until competitive markets develop.[400] CAMU suggests that the comparability standard is not met if market rates exceed the costs of providing ancillary services. Allegheny, Ohio Edison and Atlantic City support cost-based pricing for Reactive Power/Voltage Control. Ohio Edison recommends cost-based pricing for frequency regulation, and Atlantic City recommends it for scheduling and dispatch.

Several commenters suggest that the Commission require cost-based rates for ancillary services where no source other than the transmission provider exists and market-based rates for generation-related ancillary services if competition exists.[401] Washington and Oregon Energy Offices recommend that, before permitting market-based rates, at least two other non- affiliated parties should be able to offer a nearly identical ancillary service and that the Commission should use the same standards for allowing market-based rates for ancillary services that it has used for wholesale power sales. Mt. Hope Hydro argues that vertically integrated utilities should be permitted to charge cost-based rates that are limited to no more than the market price for ancillary services. It also contends that companies whose generation facilities are not supported by captive retail or transmission customers should be authorized to sell at market-based prices.

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[400] *E.g.*, Utilities For Improved Transition, Idaho, CINergy, Direct Service Industries, Mt. Hope Hydro, ABATE, TDU Systems, Missouri-Kansas Industrials, Washington and Oregon Energy Offices, IN Com.

[401] *E.g.*, PJM, Texas Utilities, Entergy, Carolina P&L.

The vast majority of commenters from all interest groups who address market-based pricing for ancillary services agree that market-based pricing is appropriate for ancillary services where competitive market conditions exist. However, commenters disagree over whether a competitive market for ancillary services currently exists.

In determining the extent of competition, many commenters distinguish between ancillary services that are (1) generation- related and (2) transmission-related. Commenters disagree over whether the Commission can declare generation-related ancillary services to be competitive on a generic basis. Many commenters contend that transmission-related ancillary services are not available in a competitive market; consequently, they agree that prices for such services should be cost-based.

Commission Conclusion

We will consider ancillary services rate proposals on a case-by-case basis.

In response to comments,[402] we offer here some general guidance on ancillary services pricing principles.

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[402]Many commenters were particularly concerned that rates for energy losses, a NOPR ancillary service, should be market-based. We need not address this concern in this Rule, however, because we will not require Real Power Losses to be offered as an ancillary service.

(1) Ancillary service rates should be unbundled from the transmission provider's rates for basic transmission service, even though such services are a necessary adjunct to basic transmission service.

(2) The fact that we have authorized a utility to sell wholesale power at market-based rates does not mean we have authorized the utility to sell ancillary services at market-based rates.

(3) In the absence of a demonstration that the seller does not have market power in such services, rates for ancillary services should be cost-based and established as price caps, from which transmission providers may offer a discount to reflect cost variations or to match rates available from any third party. If a rate **[31, 721]** discount is offered to the transmission owner itself or to an affiliate of the transmission owner, the same discounted rate must be offered to non-affiliates, as well. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory. All discounts must be posted on the transmission provider's OASIS.

(4) The amount of each ancillary service that the customer must purchase, self-supply, or otherwise procure must be readily determined from the transmission provider's tariff and comparable to the obligations to which the transmission provider itself is subject. The provider must take ancillary services for its own wholesale transmission under its own tariff.

(5) The location and characteristics of a customer's loads and generation resources may affect significantly the

level of ancillary service costs incurred by the transmission provider. Ancillary service rates and billing units should reflect these customer characteristics to the extent practicable.

6. Accounting for Ancillary Services Comments

Some commenters suggest that there may be a need for revising the Uniform System of Accounts to track better the costs of providing discrete ancillary services. Other commenters believe that ancillary services are transmission-type services and suggested that the costs of generation-provided ancillary services be refunctionalized from power production expense to transmission expense.

Oak Ridge asserts that a primary goal of those interested in restructuring the electricity industry should be to identify clearly the different functions that are today buried within the vertically integrated utility and bundled into one price. Oak Ridge, however, indicates that achieving this ideal of identifying unbundled services at appropriate prices will be difficult because of utility accounting practices.

EEI asserts that since the current Uniform System of Accounts was designed to track costs incurred to provide bundled wholesale service, it does not track the discrete costs incurred to provide ancillary services. Therefore, according to EEI, a major update is needed to support the pricing of discrete ancillary services.

ConEd states that ancillary services are integral and essential elements of providing transmission services. It notes that, historically, due to the vertical integration of utilities, those services have been bundled with the other services

provided and the costs associated with providing ancillary services have not been specifically defined. ConEd claims that to a large degree, this is due to the fact that utility accounting mechanisms were not established with the intention of identifying the costs for ancillary services.

UI asserts that if transmission customers are to be charged for certain ancillary services, it may be necessary to refunctionalize certain specific costs items from generation to transmission. UI points out that some of the reactive power to support system voltages and to provide transmission services, for example, is supplied from the variable reactive output of the generators. It states that these costs, to the extent they can be identified with the provision of transmission service, should be refunctionalized to the transmission account. However, UI states it may not be possible to develop a unit cost for specific transactions. Thus, UI states it may be more appropriate to roll these costs into the embedded transmission rate and allocate them among the various users of the transmission system.

Commission Conclusion

To ensure comparable transmission access a Transmission Provider is obligated to offer or arrange to provide certain ancillary services to the Transmission Customer. Also, the Transmission Provider may offer to provide other ancillary services to the Transmission Customer. A Transmission Customer is obligated to purchase certain ancillary services from the Transmission Provider.

Generation resources provide certain ancillary services, while transmission resources provide other ancillary

services. Consequently, the costs of providing certain ancillary services are recorded in the utility's power production expense accounts, while others are recorded in the utility's transmission expense accounts.

Currently, the Uniform System of Accounts requires that costs incurred in providing ancillary services be recorded as power production or transmission expense depending upon which resource the utility uses to supply the service. At this time, **[31,722]** we are not convinced that the amounts involved or the difficulty associated with measuring the cost of ancillary services warrants a departure from our present accounting requirements. We will specify, however, that revenues a Transmission Provider receives from providing ancillary services must be recorded by type of service in Account 447, Sales for Resale, or Account 456, Other Electric Revenues, as appropriate.

E. *Real-Time Information Networks*

In the Open Access NOPR, the Commission determined that in order to remedy undue discrimination, a utility must functionally unbundle its wholesale services, and that among the things required by functional unbundling is that the utility, when buying or selling power, rely upon the same electronic network that its transmission customers rely upon to obtain transmission information. Accordingly, the Commission accompanied its issuance of the Open Access NOPR with issuance of a notice of technical conference that initiated a proceeding in Docket No. RM95-9-000 to consider whether Real-Time Information Networks (RINS) or some other option would be the best means to ensure that potential customers of transmission services have access to the

information necessary to obtain open access transmission service on a non-discriminatory basis.[403]

The Commission affirms its conclusion that in order to remedy undue discrimination in the provision of transmission services it is necessary to have non-discriminatory access to transmission information, and that an electronic information system and standards of conduct are necessary to meet this objective. Therefore, we issue, in conjunction with this Final Rule, a final rule adding a new Part 37 that requires the creation of a basic OASIS and standards of conduct.[404]

The Phase I OASIS rules require each public utility (or its agent), as defined in section 201(e) of the Federal Power Act, 16 U.S.C. 824(e), that owns, controls, or operates facilities used for the transmission of electric energy in interstate commerce to develop and/or participate in an OASIS. The Phase I OASIS rules describe what information must be provided on the OASIS during Phase I and how OASIS must be implemented.

In addition, the new Part 37 contains a code of conduct applicable to all transmission providing public utilities. The code of conduct is designed to ensure that preferential access to information about wholesale transmission prices and

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[403]See Real-Time Information Networks, Notice of Technical Conference and Request for Comments, 60 FR 17726 (April 7, 1995).

[404]In Phase II, we will continue to develop the requirements for fully functional OASIS. We expect to issue a final rule on Phase II OASIS requirements sometime in 1997.

availability is not available to employees of the public utility engaged in wholesale marketing functions or to employees of certain of the public utility's affiliates.

F. Coordination Arrangements: Power Pools, Public Utility Holding Companies, Bilateral Coordination Arrangements, and Independent System Operators Comments

Timing of Reformation

Many marketers, IPPs, and other nonmembers of pools request that the Commission immediately apply unbundling and transmission tariff requirements to all new transactions under existing pooling agreements. APPA states that the Commission should not deal with power pools as a "follow-on activity" because treatment of pools is an integral step in achieving transmission comparability. AEC contends that until pools publish open access tariffs, the Commission should permit applications for section 211 transmission orders from one or more applicants directed to multiple respondents.

Existing pools generally urge the Commission to allow time for the pools to propose alternative structures or agreements which would meet the objectives of the final rule. EEI states that the rule may create problems for power pools that will not be examined or understood by the Commission and the public until the Commission's pooling inquiry is completed; it requests that the pooling inquiry be completed before a final rule is issued. Duke recommends that implementation of open access transmission services by power pools be addressed in a separate proceeding because implementation **[31,723]** of open access for power pools raises complex issues.

EGA, among others, argues that new transactions under existing pooling agreements should not be grandfathered, but rather should be required to meet the functional unbundling requirements of the final rule. Some pool members argue that pool transactions are largely not wholesale transactions. For example, PECO (a member of PJM) requests the Commission to clarify that the delivery of pooled generation to pool members' native load is not a "wholesale purchase" of power and thus would not require taking transmission service under one's own open access transmission tariff. Another member of PJM, BG&E, interprets the proposed rule to require all PJM economy trades to be firm point-to-point services; it claims that such a requirement "jeopardizes the continued viability of the pool."

System-Wide Tariffs

Virtually all commenters on power pool issues state that the tariff requirements should not be applied directly to individual utilities who are members of "tight" power pools. ELCON, CCEM, and others argue that the pro forma tariff requirement should be applied directly to "tight" or "single system" power pools to avoid discriminatory "pancaking" of transmission rates. However, Duke argues that where there are both multiple owners and operators, as in "loose" pools, it is appropriate to have individual tariffs unless the pool members agree otherwise. DOE recommends a power pool file a single pool-wide tariff to offset problems associated with joint ownership or control of transmission. CT DPUC recommends that the Commission provide guidance for transmission access and pricing (so as to avoid needless disruption of present methods).

Flexible Treatment

Most commenters on power pools support recognizing regional differences among power pools and urge flexibility. PSE&G (a member of PJM) states that open access tariffs must be specially crafted to deal with power pool members. NYPP and PJM state that they are considering innovations and urge that their efforts not be stifled by any final rule. CSW proposes a region-wide pricing model based on power flows. NPPD, a member of the Mid-Continent Area Power Pool (MAPP), says MAPP is considering adopting the megawatt-mile approach to transmission pricing. SoCal Edison states that California utilities are developing a market-based power pool and that it is crucial for the final rule to be flexible to permit innovations throughout the country.

ELCON and power marketers, however, argue for uniformity and point out the difficulties of moving power from system to system where each system has varying standards or "pool rules." These commenters support uniform application of the terms and conditions in the pro forma tariffs to create a national standard.

NEPOOL emphasizes that since pools remain voluntary, the imposition of rules that are not acceptable to pool members simply increases the likelihood that members will withdraw and pools will disintegrate. For this reason, NEPOOL states that solutions to enhance competition (within a tight pool setting) are best identified through the consensus of pool members, which requires both time and flexibility on the part of the Commission.

DE, DC, NJ and MD Coms emphasizes its concern that a one-size-fits-all open-access policy, while perhaps benefiting subsets of individual suppliers and purchasers, may not be the best solution for the millions of retail customers who currently rely on power pools.[405] It wants the Commission to be aware that the individual commissions have begun a formal dialog among each other and with the PJM utilities to discuss possible regional solutions to transitional competitive issues.

Open Membership

NIEP and CCEM argue that the competitive playing field cannot be level unless nonmembers receive certain power pool services on terms comparable to those for pool members. Members of pools state that "return in kind" transactions are efficient, but that such transactions are not appropriate for those entities that **[31,724]** are not similarly situated to vertically integrated utilities.

EEI maintains that those seeking the benefits of pool membership must accept the burdens imposed on existing pool members (otherwise, they would have an advantage, not comparability). EEI believes that new pool participants can negotiate and "buy into" the pool resources. Many commenters claim that unbundling certain power pool services to accommodate open access will solve the problem.

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[405] *E.g.*, DE Com, DC Com, NJ Com, MD Com.

MidAmerican states that if the Commission grants nonmembers access to pool transmission service, the Commission should allow a period of at least four years for pools to restructure and refile rate schedules to avoid the inequitable results which the Commission's requirements will impose on pool members.

MidAmerican contends that the Commission should authorize pool members to unilaterally withdraw from their pools if any restructuring or revision of rate schedules is unacceptable to the member. Holding companies

Allegheny, Southern, and other holding companies argue that coordination agreements among subsidiaries of a utility holding company system do not constitute a power pool and should not be subject to any obligations the Commission may place on power pools. Bilateral Coordination Agreements

Ohio Edison requests clarification that the Commission is not requiring new wholesale coordination transactions to be under the open access tariffs; they may be continued under existing coordination agreements. It stresses the importance of such agreements in making economy and emergency transactions.

A number of commenters agree that existing coordination contracts should not be abrogated or modified, and that transactions under these existing contracts should not be governed by the provisions of the pro forma tariffs.[406]

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[406] *E.g.*, Central Louisiana, Dayton P&L, LPPC, MEAG, Missouri Basin Group, Montana-Dakota Utilities, Nebraska Public

These commenters generally argue that existing coordination agreements should not be abrogated or amended by the final rule because: (1) they were not negotiated in the environment envisioned by the NOPR; (2) coordination sales are beneficial to consumers and ratepayers (and thus it would not be in the public interest to curtail them); and (3) the termination of coordination agreements, which in some cases have been in place for years and are tailored to parties' peculiar circumstances, could cause severe hardships in certain regions (especially with regard to scheduling and curtailment).

PSNM contends that such agreements are the result of mutually beneficial bargaining. LPPC and MEAG argue that current contracts negotiated among parties provide cost savings to consumers, which may be foregone if existing contracts are modified. Central Louisiana suggests that the pro forma tariff provisions should be flexible enough to achieve comparability if applied to both existing and new coordination agreements.

Some commenters argue that there may be cases where it is inappropriate to modify existing coordination agreements to satisfy the requirements of the rule. They assert that coordination agreements providing for emergency transactions,[407] reliability,[408] and resource efficiency gains[409]

Power District, Ohio Edison, PSNM.

[407] *E.g.*, Arizona, Ohio Edison.

[408] *E.g.*, Soyland, NRECA.

[409] *E.g.*, APPA.

need special attention. However, Soyland believes that existing agreements need to be reviewed if there is substantial increase in wholesale power market transactions, at the customer's option. TDU Systems argues that coordination contracts supporting system reliability should be honored and given scheduling and curtailment preference. TDU Systems contends that any amendments should be at the parties' discretion rather than by Commission mandate.

Several commenters suggest that the proposed rule is unclear about whether only existing transactions under agreements already approved by the Commission will be exempt from functional unbundling, or whether the proposed rule also would exempt (or grandfather) new transactions entered into pursuant to existing approved contracts.[410] Other commenters recommend that the Commission **[31,725]** clarify that its policy on unbundling applies to all new transactions, whether pursuant to new or existing agreements.[411] ConEd and KCPL request clarification that purchases made to satisfy retail service are not subject to the requirements of the pro forma tariffs.

CCEM argues that all coordination transactions, including new transactions under existing agreements, should be unbundled to ensure that transmission providers are implementing the posted transmission rate. CINergy contends that the comparability standard should be applied to existing coordination agreements, including buy-resell agreements, to

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[410] *E.g.*, APPA, CCEM, EGA.

[411] *E.g.*, APPA, CCEM, LG&E, EGA.

mitigate any unfair bulk power market advantages. Functional unbundling would ensure that a utility includes an EBB-posted transmission rate in the transaction charge. CINergy and Power Marketing Association recommend that the Commission use its authority under section 206 to require all utilities to file amendments to their existing coordination agreements providing for transmission service to be taken pursuant to the parties' open access transmission tariffs. Power Marketing Association further recommends that the Commission establish expedited procedures to address the situation arising from conflicting pro forma tariffs and existing coordination provisions.

Tallahassee also believes that the comparability standard should be applied to existing coordination agreements, but Tallahassee recommends that the Commission establish a transition period to allow for renegotiation among parties rather than imposing modifications to existing agreements. Renegotiation would provide an opportunity to retain previously bargained-for benefits. Detroit Edison also contends that many of the existing coordination agreements do not provide for the services required under the pro forma tariffs. Like Tallahassee, Detroit Edison recommends that the Commission allow sufficient time for parties to renegotiate existing agreements. CINergy suggests a three-year transition period.

Coordination Pricing Practices

EEI and PJM disagree with the Commission's assertion that current coordination pricing is no longer just and reasonable in the absence of an open access tariff. Ohio Edison and PA Com question the basis of the Commission's

preliminary conclusion that current coordination pricing is no longer justified in the absence of a seller's tariff offer of non-discriminatory open access transmission services. PA Com asserts that the Commission's underlying assumption of general lack of transmission access by wholesale customers has not been established as fact in the proposed rule.

MN DPS supports current coordination pricing methods provided that utilities have executed open-access tariffs. Missouri Basin Group argues that, if increased market competition materializes through open access, utilities will decreasingly rely on current coordination pricing if it no longer produces the most beneficial outcome. Missouri Basin Group recommends the Commission simply allow utilities to choose a pricing method even if a utility opts for a less beneficial outcome. Nebraska Public Power District also urges the Commission to avoid mandating coordination pricing methods. Nebraska Public Power District is concerned that this may impede establishing RTGs where such pricing is by mutual agreement and subject to ADR procedures.

Several commenters agree that current coordination pricing may no longer be appropriate in an open access regime.[412] FL Com believes that current coordination pricing should be replaced by market-based rates if open access transmission service is imposed by the Commission.

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[412] *E.g.*, Arizona, CINergy, Consumers Power, EEI, PJM.

Commission Conclusion

The term "coordination" is applied to a wide variety of wholesale power sales agreements within the industry, including interchange, interconnection, pooling, and other agreements. Broadly speaking, any non-requirements power sales agreement can be considered to be a coordination agreement.[413]

The Final Rule's general requirement for non-discriminatory transmission access **[31,726]** and pricing by public utilities, and its specific requirement that public utilities unbundle their transmission rates and take transmission service under their own tariffs, apply to all public utilities' wholesale sales and purchases of electric energy, including coordination transactions. The Commission has determined that certain existing wholesale coordination arrangements and agreements must be modified to ensure that necessary transmission services for such arrangements and agreements are taken under open access transmission tariffs and thus that such arrangements and agreements are not unduly discriminatory. Below we discuss how and when various types of coordination agreements will need to be modified, and when public utility parties to coordination agreements must begin to trade power under those agreements using transmission service obtained under the same open access transmission tariff available to non-parties.

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[413]For example, a 30-year contract to supply 50 MW of power can be considered to be a coordination arrangement because it is not a contract to meet all of the buyer's power requirements.

Coordination arrangements, and the agreements governing them, vary widely. They range from relatively simple bilateral arrangements to complex tight power pools. Our discussion addresses four broad categories of arrangements and accompanying agreements: "tight" power pools, "loose" power pools, public utility holding company arrangements, and bilateral coordination arrangements. For purposes of implementing the non- discriminatory, open access requirements of the Final Rule, we are dividing bilateral coordination agreements into two general categories: bilateral economy energy agreements and other bilateral coordination agreements. Economy energy agreements typically provide for short-term economy trading "if, as, and when available" and are generally driven by the buyer and seller's generation costs. They do not require either the seller or the buyer to engage in a particular transaction. Other coordination agreements are typically longer term or open-ended. Some may involve joint ownership or joint planning of generation.[414] Others may provide joint operation of facilities so that the parties can coordinate their maintenance schedules or provide one another with emergency service. These longer-term coordination agreements are distinguished from short-term economy trading agreements in that the parties have undertaken a contractual obligation to operate their facilities so as to support one another under the conditions specified in the arrangements.

As noted in the NOPR, power pools, in contrast to most bilateral arrangements, present complex issues that may

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[414] Agreements dealing with joint ownership or operation of transmission facilities are discussed at Section IV.C.3.

require special implementation requirements.[415] This is because these arrangements may involve agreements containing an intricate set of rights, obligations, and considerations among the members of a pool. We provide for implementation requirements herein that vary depending upon the type of "pooling" arrangement involved.

The Commission has concluded that in order to adequately remedy the undue discrimination in transmission access and pricing by public utilities that are members of power pools or other coordination arrangements, such public utilities must remove preferential transmission access and pricing provisions from agreements governing their transactions. The filing of open access tariffs by the public utility members of a power pool is not enough to cure undue discrimination in transmission if those public utilities can continue to trade with a selective group within a power pool that discriminatorily excludes others from becoming a member and that provides preferential intra-pool transmission rights and rates. The same holds true of certain bilateral arrangements that allow preferential transmission pricing or access. These arrangements and agreements need to be changed. We expect such arrangements and agreements to be **[31,727]** modified by the dates indicated in this Rule.

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[415]The Commission did not define what it meant by "power pools" in the NOPR discussion. We use the term power pool in a very broad context here and have generally characterized three broad types of arrangements that represent some form of pooling: "tight pools", "loose" pools and other multilateral coordination arrangements, and holding companies. Even between the categories of tight and loose pools, however, there is no bright dividing line.

However, if necessary, we will institute section 206 proceedings against public utilities that do not make such filings.

The Commission's technical conferences on power pools, ISOs, and pro forma tariffs made clear to us the need to articulate guidance in this Rule on the restructuring or modification of unduly discriminatory coordination arrangements -- particularly tight power pools.[416] They also made clear that members of tight power pools, in particular, need time to make the necessary modifications to these arrangements. We recognize that members of some power pools are already in the process of formulating voluntary modifications to pooling agreements to be filed with the Commission (e.g., PJM, NYPP, NEPOOL). Therefore, we will provide adequate time for these filings as well as guidance to changes that need to be made.

In addition, although we do not at this time find it necessary to require power pools to form an independent system operator in order to remedy undue discrimination, we believe ISOs may prove to be an effective means for accomplishing comparable access.[417] We recognize that

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[416]A technical conference on pro forma tariffs was held on October 27, 1995. A technical conference on power pools was held on December 5 and 6, 1995 and a follow-up technical conference on ISOs and power pools was held on January 24, 1996.

[417]The DOJ and DOE suggested that the Commission examine operational unbundling as a way of enforcing comparability in transmission service. DOJ and DOE believe that functional unbundling may not be adequate to ensure comparability

several utilities are exploring the possibility of forming ISOs. For example, discussions are ongoing in California, PJM, NYPP, and the Midwest. Therefore, because of the industry's interest (which we share) in the concept of an ISO and the potential for an ISO to provide non-discriminatory transmission services to all market participants, we will provide guidance in this section on minimum ISO characteristics.

1. Tight Power Pools

For purposes of this Rule, the tight power pools are: New York Power Pool (NYPP), New England Power Pool (NEPOOL), Pennsylvania-New Jersey-Maryland Interconnection (PJM), and the Michigan Electric Coordinated Systems (MECS).

Public utilities who are members of a tight pool must file, within 60 days of publication of the Final Rule in the Federal Register, either: (1) an individual Final Rule pro forma tariff; or (2) a joint pool-wide Final Rule pro forma tariff. They are not required to take service for pool transactions under the tariff that is filed within 60 days. However, they will be required to file a joint pool-wide Final Rule pro forma tariff no later than December 31, 1996, and must begin to take service under that tariff for all pool

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and so have recommended that some form of operational unbundling be required. While we believe that requiring this is premature, we note that an ISO is one way to achieve operational unbundling and we encourage the voluntary development of ISOs.

transactions no later than December 31, 1996. The purpose of this extension is to allow sufficient time for tight pools to amend their pooling agreements and to restructure their operations to conform to the requirements of the Final Rule. We also believe that the additional time is necessary to preserve efficient trading arrangements during the restructuring period.

The Commission therefore will require that the public utility members of tight pools file reformed power pooling agreements no later than December 31, 1996. The reformed power pool agreements should establish open, non-discriminatory membership provisions (including establishment of an ISO, if that is a pool's preferred method of remedying undue discrimination) and modify any provisions that are unduly discriminatory or preferential. The membership provision must allow any bulk power market participant to join, regardless of the type of entity, affiliation, or geographic location.

If the reformed agreement allows members to make transmission commitments or contributions in exchange for the discounted transmission rates, the pool may file a transmission tariff that contains an access fee for non-transmission owning members or non-members, justified solely on the basis of transmission-related costs. Alternatively, the pool could make available **[31,728]** a transmission rate that is structured the same as the discounted rate (e.g., non-pancaked) but with a higher rate that is justified on the basis of transmission-related costs borne (or contributed) by the pool members. However, any such access fee or higher rate must be justified solely on the basis of transmission costs and cannot be tied to the costs of any other

agreement among the pool members (e.g., generation reserve sharing).

2. Loose Pools

For purposes of the Final Rule, a loose pool is any multi- lateral (more than 2 public utilities) arrangement, many of which contain discounted and/or special transmission arrangements. Examples are MAPP, Inland Power Pool, and the MOKAN pool. Other entities may qualify to be treated as a loose pool if they can show that they meet the definition above.

Public utilities within a loose pool must file, within 60 days of publication of the Final Rule in the Federal Register, either: (1) an individual Final Rule pro forma tariff; or (2) a pool-wide Final Rule pro forma tariff. They are not required to take service for pool transactions under the tariff that is filed within 60 days. However, they will be required to file a joint pool-wide Final Rule pro forma tariff no later than December 31, 1996, and must begin to take service under that tariff for all pool transactions no later than December 31, 1996. The purpose of this extension is to allow sufficient time for loose pools to amend their agreements and to restructure their operations to conform to the requirements of the Final Rule. We also believe that the additional time is necessary to preserve efficient trading arrangements during the restructuring period.

The Commission therefore will require that the public utility members of loose pools file reformed power pooling agreements no later than December 31, 1996. They also must file a joint pool-wide tariff no later than December 31, 1996.

The reformed power pool agreements should establish open, non-discriminatory membership provisions and modify any provisions that are unduly discriminatory or preferential. The membership provision must allow any bulk power market participant to join, regardless of the type of entity, affiliation, or geographic location.

The Commission recognizes that loose pools typically do not operate as a single control area and that operational unbundling, perhaps through an ISO, might not be readily attainable at this time. Nonetheless, we encourage the members of loose pools to explore the advantages of the ISO concept.

If the reformed agreement allows members to make transmission commitments or contributions in exchange for discounted transmission rates, the pool may file a transmission tariff that contains an access fee for non-transmission owning members or non-members, justified solely on the basis of transmission-related costs. Alternatively, the pool could make available a transmission rate that is structured the same as the discounted rate (e.g., non-pancaked) but with a higher rate that is justified on the basis of transmission-related costs borne (or contributed) by the pool members. However, any such access fee or higher rate must be justified solely on the basis of transmission costs and cannot be tied to the costs of any other agreement among the pool members (e.g., generation reserve sharing).

3. Public Utility Holding Companies

Public utility members of registered and exempt holding companies that are also members of tight or loose

pools are subject to the tight and loose pool requirements set forth above. The remaining holding company public utility members, with the exception of the Central and South West (CSW) System, are required to file a single system-wide Final Rule pro forma tariff permitting transmission service across the entire holding company system at a single price within 60 days of publication of the Final Rule in the Federal Register (service companies may, of course, file on behalf of their public utility affiliates). As discussed below, CSW presents special circumstances.

The CSW System is comprised of four operating public utilities. Two of those utilities, Southwestern Electric Power Company (SWEPCO) and Public Service Company of Oklahoma (PSO) operate in the Southwest Power Pool (SPP). The other two, West Texas Utilities Company (West Texas) and Central Power and Light Company (CP&L), operate in the Electric Reliability Council of Texas (ERCOT). SWEPCO and PSO exchange power with West Texas and CP&L **[31,729]** through two high voltage, direct current interconnections (the North and East Interconnections).[418]

Pursuant to the Commission orders concerning the North and East Interconnections, CP&L, West Texas, SWEPCO, and PSO have on file what are referred to as the

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[418]The North and East Interconnections were ordered by the Commission pursuant to sections 210, 211 and 212 of the Federal Power Act. See *Central Power and Light Company, et al.*, 17 FERC ¶61,078 (1981), order on reh'g, 18 FERC ¶61,100 (1982); 40 FERC ¶61,077 (1987).

"to or from and over tariffs."[419] Those tariffs apply only to transmission service that involves the delivery of power and energy to or from and over the North and East Interconnections.[420] The tariffs do not apply to the transmission of power for CSW subsidiaries other than the operating companies. The tariffs in many respects are different from the Final Rule pro forma tariff and do not provide comparable services. Moreover, the pricing provided in the "to or from and over" tariffs is different from the pricing set forth in the Texas Commission's final open access rule.[421]

Given these special circumstances, we believe it appropriate to give CSW the opportunity to propose a solution to achieving comparability for the CSW system. Accordingly,

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[419]Houston Lighting and Power Company (HL&P) and Texas Utilities Electric Company (TU) also have on file "to or from and over tariffs" pursuant to the Commission orders.

[420]*See, e.g.*, CP&L and West Texas Interpool Transmission Service Tariff, §4.1.

[421]Compare 21 TEX REG 1397, LEXIS, mimeo at p. 18 (adopting hybrid pricing scheme with 70% of transmission rate based on regional postage stamp method and 30% based on the vector-absolute megawatt-mile method) with Id. at Article III.

We note that the Texas Commission concluded that the ERCOT portion of the costs of the North and East Interconnections "should be included in the cost of service, when the owners of the (Interconnections) amend the FERC tariffs for the use of the (Interconnections) to provide equal access to other utilities. 21 TEX REG, LEXIS, mimeo at p. 24.

we direct the public utility subsidiaries of CSW to consult with the Texas, Arkansas, Oklahoma and Louisiana Commissions and to file not later than December 31, 1996 a system tariff that will provide comparable service to all wholesale users on the CSW System,[422] regardless of whether they take transmission service wholly within ERCOT or the SPP, or take transmission service between the reliability councils over the North and East Interconnections.[423]

The Commission will give public utilities that are members of holding companies an extension of the requirement to take service under the system tariff for wholesale trades between and among the public utility operating companies within the holding company system. This extension is until December 31, 1996 -- the same extension we are granting to power pools. At that point, the public utility operating companies will be required to take service

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[422]It may be appropriate to have different rates for transmission service wholly within ERCOT or the SPP, and for service between the reliability councils. However, the same rates, terms, and conditions applicable for third parties should also be applicable to the CSW System's wholesale transmission requirements.

[423]We recognize that this action may require amendment to the Commission's orders under FPA sections 210, 211, and 212, ordering the North and East Interconnections. In this regard, it should be clearly understood that the Commission's action in requiring comparable service by the CSW System is not in any way intended to result in public utility status to any ERCOT participants that are not public utilities -- e.g., HL&P and TU. See 16 U.S.C. 824(b)(2).

under the Final Rule pro forma tariff for wholesale trades among themselves. In addition, it may be necessary for registered holding companies to reform their holding company equalization agreement to recognize the non-discriminatory terms and conditions of transmission service required under the Final Rule pro forma tariff.

4. Bilateral Coordination Arrangements

Any bilateral wholesale coordination agreement executed after the effective date of this Rule will be subject to the functional unbundling and open access requirements set forth in this Rule. With regard to existing bilateral agreements, however, the diversity of the types of agreements currently on file presents special implementation problems. The Commission is particularly concerned with future economy energy transactions that may occur pursuant to existing umbrella-**[31,730]**type coordination agreements. Accordingly, we shall require all bilateral economy energy coordination contracts executed before the effective date of this Rule to be modified to require unbundling of any economy energy transaction occurring after December 31, 1996. All non- economy energy bilateral coordination contracts executed before the effective date of this Rule will be permitted to continue in effect, but will be subject to complaints filed under section 206 of the FPA. Under those procedures, the rates, terms, and conditions of individual coordination contracts may be challenged as unduly discriminatory or otherwise unlawful.

To compute the unbundled coordination compliance rate, the utility must subtract the corresponding transmission unit charge in its open access tariff from the existing

coordination rate ceiling. For example, if a utility has a coordination rate ceiling for hourly service of incremental cost plus 15 mills/kWh and a transmission tariff rate for hourly service of 3 mills/kWh, it shall revise the coordination rate ceiling to incremental cost plus 12 mills/kWh. The Commission cautions that the compliance filing will be strictly limited to removing the current transmission tariff price from the coordination price and will not be a medium for otherwise revising the residual coordination sales price.

The transmission rate for the coordination transactions may be at or below the tariff rate. However, if a utility's transmission operator offers a discounted transmission rate to the utility's wholesale marketing department or an affiliate for the purposes of coordination transactions, the same discounted rate must be offered to others for trades with any party to the coordination agreement. In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory.[424] This may require parties to file modifications of the coordination arrangements.

ISO Principles

The Commission recognizes that some utilities are exploring the concept of an Independent System Operator and that the tight power pools are considering restructuring proposals that involve an ISO. While the Commission is not requiring any utility to form an ISO at this time, we wish to encourage the formation of properly-structured ISOs. To this

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[424]All discounts must be posted on the transmission provider's OASIS.

end, we believe it is important to give the industry some guidance on ISOs at this time. Accordingly, we here set out certain principles that will be used in assessing ISO proposals that may be submitted to the Commission in the future.

These principles are applicable only to ISOs that would be control area operators, including any ISO established in the restructuring of power pools. We recognize that some utilities are exploring concepts that do not involve full operational control of the grid. Without in any way prejudging the merits of such arrangements, the following principles do not apply to independent administrators or coordinators that lack operational control. We do not have enough information at this time to offer guidance about such entities, but recognize that they could perform a useful role in a restructured industry.

Because an ISO will be a public utility subject to our jurisdiction,[425] the ISO's operating standards and procedures must be approved by the Commission. In addition, a properly constituted ISO is a means by which public utilities can comply with the Commission's non-discriminatory transmission tariff requirements. The principles for ISOs are:

1. The ISO's governance should be structured in a fair and non-discriminatory manner. The primary purpose of an

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[425]A public utility is any person that owns or operates facilities used for the transmission of electric energy in interstate commerce or the sale of electric energy at wholesale in interstate commerce. An ISO will operate facilities used for the transmission of electric energy in interstate commerce and thus will be subject to the Open Access and OASIS rules.

ISO is to ensure fair and non-discriminatory access to transmission services and ancillary services for all users of the system. As such, an ISO should be independent of any individual market participant or any one class of participants (e.g., transmission owners or end-users). A governance structure that includes fair representation **[31,731]** of all types of users of the system would help ensure that the ISO formulates policies, operates the system, and resolves disputes in a fair and non-discriminatory manner. The ISO's rules of governance, however, should prevent control, and appearance of control, of decision-making by any class of participants.

2. An ISO and its employees should have no financial interest in the economic performance of any power market participant. An ISO should adopt and enforce strict conflict of interest standards. To be truly independent, an ISO cannot be owned by any market participant. We recognize that transmission owners need to be able to hold the ISO accountable in its fiduciary role, but should not be able to dictate day-to-day operational matters. Employees of the ISO should also be financially independent of market participants. We recognize, however, that a short transition period (we believe 6 months would be adequate) will be needed for employees of a newly formed ISO to sever all ties with former transmission owners and to make appropriate arrangements for pension plans, health programs and so on. In addition, an ISO should not undertake any contractual arrangement with generation or transmission owners or transmission users that is not at arm's length. In order to ensure independence, a strict conflict of interest standard should be adopted and enforced.

3. An ISO should provide open access to the transmission system and all services under its control at non-pancaked rates pursuant to a single, unbundled, grid-wide tariff that applies to all eligible users in a non-discriminatory manner. An ISO should be responsible for ensuring that all users have non-discriminatory access to the transmission system and all services under ISO control. The portion of the transmission grid operated by a single ISO should be as large as possible, consistent with the agreement of market participants, and the ISO should schedule all transmission on the portion of the grid it controls. An ISO should have clear tariffs for services that neither favor nor disfavor any user or class of users.

4. An ISO should have the primary responsibility in ensuring short-term reliability of grid operations. Its role in this responsibility should be well-defined and comply with applicable standards set by NERC and the regional reliability council. Reliability and security of the transmission system are critical functions for a system operator. As part of this responsibility an ISO should oversee all maintenance of the transmission facilities under its control, including any day-to-day maintenance contracted to be performed by others. An ISO may also have a role with respect to reliability planning. In any case, the ISO should be responsible for ensuring that services (for all users, including new users) can be provided reliably, and for developing and implementing policies related to curtailment to ensure the on-going reliability and security of the system.

5. An ISO should have control over the operation of interconnected transmission facilities within its region. An

ISO is an operator of a designated set of transmission facilities.

6. An ISO should identify constraints on the system and be able to take operational actions to relieve those constraints within the trading rules established by the governing body. These rules should promote efficient trading. A key function of an ISO will be to accommodate transactions made in a free and competitive market while remaining at arm's length from those transactions. The ISO may need to exercise some level of operational control over generation facilities in order to regulate and balance the power system, especially when transmission constraints limit trading over interfaces in some circumstances. It is important that the ISO's operational control be exercised in accordance with the trading rules established by the governing body. The trading rules should promote efficiency in the marketplace. In addition, we would expect that an ISO would provide, or cause to be provided, the ancillary services described in this Rule.

7. The ISO should have appropriate incentives for efficient management and administration and should procure the services needed for such management and administration in an open competitive market. Management and administration of the ISO should be carried out in an efficient manner. In addition to personnel and administrative functions, an ISO could perform certain operational functions, such as: determination of appropriate system expansions, transmission **[31,732]** maintenance, administering transmission contracts, operation of a settlements system, and operation of an energy auction. The ISO should use competitive procurement, to the extent possible, for all services provided by the ISO that are

needed to operate the system. All procedures and protocols should be publicly available.

8. An ISO's transmission and ancillary services pricing policies should promote the efficient use of and investment in generation, transmission, and consumption. An ISO or an RTG of which the ISO is a member should conduct such studies as may be necessary to identify operational problems or appropriate expansions. Appropriate price signals are essential to achieve efficient investment in generation and transmission and consumption of energy. The pricing policies pursued by the ISO should reflect a number of attributes, including affording non-discriminatory access to services, ensuring cost recovery for transmission owners and those providing ancillary services, ensuring reliability and stability of the system and providing efficient price signals of the costs of using the transmission grid. In particular, the Commission would consider transmission pricing proposals for addressing network congestion that are consistent with our Transmission Pricing Policy Statement. In addition, an ISO should conduct such studies and coordinate with market participants including RTGs, as may be necessary to identify transmission constraints on its system, loop flow impacts between its system and neighboring systems, and other factors that might affect system operation or expansion.

9. An ISO should make transmission system information publicly available on a timely basis via an electronic information network consistent with the Commission's requirements. A free-flow of information between the ISO and market participants is required for an ISO to perform its functions and for market participants to efficiently participate in the market. At a minimum,

information on system operation, conditions, available capacity and constraints, and all contracts or other service arrangements of the ISO should be made publicly available. This information should be made available on an OASIS operated by the ISO.

10. An ISO should develop mechanisms to coordinate with neighboring control areas. An ISO will be required to coordinate power scheduling with other entities operating transmission systems. Such coordination is necessary to ensure provision of transmission services that cross system boundaries and to ensure reliability and stability of the systems. The mechanisms by which ISOs and other transmission operators coordinate can be left to those parties to determine.

11. An ISO should establish an ADR process to resolve disputes in the first instance. An ISO should provide for a voluntary dispute resolution process that allows parties to resolve technical, financial, and other issues without resort to filing complaints at the Commission. We would encourage the ISO to establish rules and procedures to implement alternative dispute resolution processes.

G. *Pro Forma Tariff*

In the NOPR, the Commission stated that --

all utilities use their own systems in two basic ways: to provide themselves point-to-point transmission service that supports coordination sales, and to provide themselves network transmission service that supports the economic dispatch of their own generation units and purchased power

resources (integrating their resources to meet their internal loads).[426]

Accordingly, the Commission proposed two pro forma tariffs in Appendices B and C of the NOPR: one for point-to-point service and one for network service. Our goal was to encourage the development of competitive bulk power markets by ensuring that all participants would be able to secure transmission services on a non-discriminatory basis. We attempted in the NOPR pro forma tariffs to articulate the minimally acceptable terms and conditions of service for point-to-point and network transmission service that were required to ensure non-discriminatory transmission service.[427] We explained that, for the most part, specific pricing provisions were omitted. We asked for **[31,733]** comments on whether these tariffs provided a good basis for defining the minimum acceptable non-price terms and conditions of service.[428]

Subsequently, in a June 28, 1995 order, we encouraged public utilities to file open access transmission tariffs as soon as possible.[429] Tariffs with terms and conditions of service substantively similar to the NOPR pro forma tariffs

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[426]*FERC Statutes and Regulations* ¶32,514 at p. 33,079.

[427]*Id.* at p. 33,092.

[428]On October 27, 1995, the Commission's staff sponsored a technical conference on the pro forma tariffs.

[429]*American Electric Power Service Corporation, et al.*, 71 FERC ¶61,393, modified, 72 FERC ¶61,287 (1995).

would become effective without a refund condition, assuming there were no other concerns, e.g., rate issues. We also indicated that these tariffs would be subject to revision based on the Final Rule.

Unified Pro Forma Tariff

The Commission received many comments on both the point-to-point and network tariffs. Many commenters suggested improvements to the proposed tariffs. Others took issue with how to reconcile various aspects of service under the two tariffs (e.g., cost allocation, service priority, customer rights and obligations). As discussed below, the Commission has attempted to address these concerns in developing tariff requirements for the Final Rule. Importantly, while the Commission has retained point-to-point transmission service and network transmission service as distinct services, the requirements for the two services are now in a single pro forma tariff.[430] The Final Rule pro forma tariff eliminates many of the differences between the two NOPR pro forma tariffs, provides a unified set of definitions, and consolidates certain common requirements such as the obligation to provide ancillary services. The general terms and conditions of transmission service specified in the Final Rule pro forma tariff should be familiar to all utilities, particularly those that have voluntarily filed open access tariffs based on the NOPR pro forma tariffs.

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[430]The Final Rule pro forma tariff is attached as Appendix D.

The Commission believes that the modified, single pro forma tariff, in conjunction with the other requirements, is sufficient to remedy undue discrimination in the provision of transmission services. However, we note that in an accompanying notice of proposed rulemaking in Docket No. RM96-11-000, we are seeking comments on whether a different form of open access tariff -- one based solely on a capacity reservation system -- might better accommodate competitive changes occurring in the industry while ensuring that all wholesale transmission service is provided in a fair and non-discriminatory manner.

We address below the comments received on the NOPR tariff and the specific modifications we have made in the Final Rule pro forma tariff.

1. Tariff Provisions That Affect The Pricing Mechanism

a. Non-Price Terms and Conditions Comments

Utilities For Improved Transition argues that any generic imposition of detailed tariffs on the electric industry will stifle the evolution of the industry. Rather, it asserts, utilities that supply transmission service should be permitted to apply general principles of comparability in their company-specific tariffs, using terms and conditions of service based on their own particular circumstances and those of their customers.

Utility Working Group wants the final rule to allow utilities to depart from the pricing method implicitly contained in the NOPR pro forma tariffs. It argues that the final rule

should recognize that some terms and conditions may not make sense in the context of innovative pricing proposals.

DOE thinks that it is proper to base the tariffs on a familiar and simple pricing method. However, DOE suggests that, in the future, the Commission carefully assess the workability of the contract path model in a competitive bulk power market. DOE suggests that spot or real-time pricing should be considered.

Numerous commenters contend that the NOPR pro forma tariffs are based upon the contract path, embedded cost methodology. According to EEI and other IOU commenters, conforming changes may be needed to various terms and conditions **[31,734]** of the tariffs to implement pricing methodologies that are not based upon contract path. These commenters argue that any flow-based model would necessitate different non-price terms and conditions. The commenters generally recognize the technical difficulties of implementing a flow-based model.[431] These commenters assert that the NOPR pro forma tariffs, as written, are not independent of pricing.

EGA criticizes the assumption underlying the contract path approach, i.e., that the capacities of individual transmission paths can be determined independently and made available to third parties. EGA notes that, in light of the competitive implications associated with transmission pricing, some utilities may propose other non-price terms and

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[431] Additional comments concerning transition to flow-based pricing are summarized in Section IV.A.6.

conditions suitable for other pricing methods, including power-flow-based tariffs. EGA expresses concern that the pro forma tariffs will be the only type of tariff allowed. EGA believes that the Commission should follow its transmission pricing policy guidelines and not impose a special burden on parties proposing tariffs that differ from the final rule pro forma tariffs, including non-price terms that support alternative pricing methods.

Some commenters also interpret the lack of reference to opportunity cost and incremental cost in the NOPR pro forma tariffs as a rejection of their use.[432]

Commission Conclusion

We agree that non-price terms and conditions cannot be designed independent of pricing and cost recovery. As discussed in detail below, the Final Rule pro forma tariff is intended to initiate open access, with non-price terms and conditions based on the contract path model of power flows and embedded cost ratemaking. It is designed based on the practices and procedures currently used by virtually all public utilities and complements the large number of tariffs already filed with the Commission. The Final Rule pro forma tariff is not intended to signal a preference for contract path/embedded cost pricing for the future. We recognize that the industry, in response to changes in institutions, competitive pressure, and technological innovations, is evolving rapidly. For example, various forms of flow-based pricing are beginning to be

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[432]*E.g.*, BPA, Utilities For Improved Transition, PG&E, Duke.

considered in conjunction with electronic transmission information systems. We seek to encourage this process and will in the future entertain non- discriminatory tariff innovations to accommodate new pricing proposals.[433]

In response to various comments, we are revising certain non-price terms and conditions where suggested changes either improve the tariff services or reconcile tariff inconsistencies. The nature of these tariff revisions does not appear to have serious cost consequences. The mandated changes are generally compatible with the rate proposals already filed by many public utilities. As discussed in Section IV.H., those utilities will not be required to file corresponding rate changes due to our mandated tariff changes to non-price terms and conditions, although they will be permitted to do so.

The Final Rule pro forma tariff includes specific terms and conditions rather than general principles. By initially requiring a standardized tariff,[434] we intend to foster broad access across multiple systems under standardized terms and conditions. However, in response to concerns raised by certain commenters, the tariff provides for certain deviations where it can be demonstrated that unique practices in a geographic region require modifications to the Final Rule pro

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[433]We further clarify that, contrary to some commenters' interpretation, the Final Rule pro forma tariff is in no way a rejection of opportunity or incremental cost pricing.

[434]As noted in Section IV.H., public utilities may propose variations that are consistent with or superior to the terms and conditions in the Final Rule pro forma tariff.

forma tariff provisions. Accordingly, where applicable, the tariff permits the use of alternative non-price terms or conditions that are reasonable, generally accepted in the region, and consistently adhered to by the transmission provider.

Finally, we will allow utilities to propose a single cost allocation method for network and point-to-point transmission services. These principles, as well as other **[31,735]** modifications and clarifications to the NOPR pro forma tariffs, are discussed in detail below.

b. Load Ratio Sharing Allocation Mechanism for Network Service

Comments

Some commenters believe that load ratio cost allocation is appropriate for network service.[435] Other commenters argue that load ratio cost allocation is inappropriate, but disagree on the alternative. They offer a variety of other cost allocation and pricing methods.

The most frequent comment is that network and point-to-point services should be priced on the same basis. Florida Power Corp wants network contract demand to be offered and priced on a 12 CP basis.[436] ConEd and Duke argue that their

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[435]*E.g.*, PSNM, WP&L.

[436]Florida Power Corp's contract demand proposal would allow a network customer to nominate less than its full load for transmission service.

systems are built and designed to meet a single peak; therefore, they contend that network service costs should be allocated with a load ratio calculation based on annual system peak rather than 12 CP. PSE&G claims that load ratio cost allocation works only if the customer has its own generation. Many commenters propose that "behind the meter" generation and load be eliminated from the network load ratio calculation.[437]

CINergy notes that the transmission provider's monthly load ratio calculation includes its long-term off-system firm service. It proposes that off-system sales be eliminated from the load ratio calculation to enable the transmission provider to offer discounts on long-term service. Alternatively, CINergy proposes that the revenues from these long-term off-system sales be shared with network customers based on their load ratio.

Atlantic City and Allegheny contend that cost allocation for network service should also reflect customers' relative energy use (i.e., not just customers' coincident demand). Consequently, these commenters propose that cost allocation consider the network customer's actual load factor. Allegheny also proposes adding a minimum revenue provision to the load ratio method to recognize cost responsibility for non-peak use. Allegheny further proposes to include an increasing return on equity as available transmission capacity decreases. EEI proposes that cost allocation be based on a customer's non-coincident peak demand.

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[437] *E.g.*, Cajun, NRECA.

Lower Colorado River Authority proposes using load flow studies to determine planned use during the system peak with MW-mile billing units. It believes that this pricing method should be used for all transmission service to ensure comparable transmission pricing. Oklahoma G&E wants cost allocation to be based on the impacted MW-mile method, or alternatively, to determine embedded cost by voltage level. Centerior proposes the use of actual transfer capability instead of contract path capability in determining cost responsibility.

Orange & Rockland recommends some form of a "poolco" approach using locational marginal cost pricing. DOE also recommends using location-specific spot pricing (a form of marginal cost) for operating and congestion costs.

Public Generating Pool believes that load ratio share pricing is unworkable in the Pacific Northwest, in part because generation is generally located outside of the control area directly served by parties in the Northwest, and in part because BPA, which does not have a typical service territory, dominates the regional transmission market. Seattle states that cost allocation based solely on demand is inappropriate for systems that consist predominantly of hydro generation.[438]

AEC & SMEPA and NRECA are concerned about pancaked rates for network service that is provided to load served by more than one network tariff. Other commenters

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[438]Additional comments concerning the Pacific Northwest are summarized in Section IV.K.

advocate use of some form of regional pricing.[439] American Wind proposes the use of a complex seasonal calculation, which appears to benefit wind energy. NY Com and Missouri-Kansas Industrials also express a preference for seasonal pricing models.

[31,736]
Commission Conclusion

We conclude that the load ratio allocation method of pricing network service continues to be reasonable for purposes of initiating open access transmission. Network service permits a transmission customer to integrate and economically dispatch its resources to serve its load in a manner comparable to the way that the transmission provider uses the transmission system to integrate its generating resources to serve its native load. Because network service is load based, it is reasonable to allocate costs on the basis of load for purposes of pricing network service. This method is familiar to all utilities, is based on readily available data, and will quickly advance the industry on the path to non-discrimination. We are reaffirming the use of a twelve monthly coincident peak (12 CP) allocation method because we believe the majority of utilities plan their systems to meet their twelve monthly peaks. Utilities that plan their systems to meet an annual system peak (e.g., ConEd and Duke) are free to file another method if they demonstrate that it reflects their transmission system planning. Moreover, we recognize that alternative allocation proposals may have merit and welcome

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[439] *E.g.*, OH Coops, Municipal Energy Agency Nebraska, UT Com.

their submittal by utilities in future rate applications. They will be evaluated on a case-by-case basis and decided on their merits.

As to the concerns raised by AEC & SMEPA and NRECA about pancaked rates for network service provided to load served by more than one network service provider, we have stated that if a customer wishes to exclude a particular load at discrete points of delivery from its load ratio share of the allocated cost of the transmission provider's integrated system, it may do so.[440] Customers that elect to do so, however, must seek alternative transmission service for any such load that has not been designated as network load for network service. This option is also available to customers with load served by "behind the meter" generation that seek to eliminate the load from their network load ratio calculation.

As noted, the most frequent comment is that the network and point-to-point services should be priced on a similar basis. This concern is addressed in the next section.

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[pp. 31,743 - 31,753]

[31,743]

g. Ceiling Rate for Non-Firm Point-to-Point Service

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[440] *Florida Municipal Power Agency v. Florida Power & Light Company*, 74 FERC ¶61,006 (1996), reh'g pending.

Commenters generally support a ceiling rate for non-firm transmission service, capped at the firm rate.[453] Others request clarification as to whether the point-to-point tariff rates are fixed or are ceiling rates. Central Illinois Public Service's major concern is that, if the rates are fixed, the tariffs may result in higher prices for capacity and energy than those currently allowed for bundled service.

NYSEG argues that unequal pricing is a natural phenomenon of the open marketplace and requests assurance that offering transmission service at prices below a cost-based ceiling rate will not expose a transmission provider to claims of undue discrimination.

AEC & SMEPA opposes using the firm rate as the cap for non-firm transmission service. It states that, given the substantially lower quality of non-firm service (with no obligation to plan for such service), no cost-of-service principle justifies charging rates for non-firm service as high as the rate for firm service.

EGA and NRECA state that any discounts from the maximum firm rate must be uniform, transparent, readily understood, and posted on a RIN. According to CCEM and NRECA, the transmitting utility must have nondiscriminatory discount practices and must contemporaneously offer discounts to transmission customers at the same time and on the same basis as discounts for internal sales operations or affiliates. Commission Conclusion

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[453] *E.g.*, Duke, SCE&G, AEP, FPL.

We believe that it is important to continue to allow pricing flexibility. In accordance with the Commission's current policies, the rate for non-firm point-to-point transmission service may reflect opportunity costs. Any provisions for opportunity cost pricing for non-firm service must meet the requirements already discussed. If a utility chooses to adopt opportunity cost pricing, the non-firm rate is effectively capped by the availability of firm service and is not subject to a separately-stated price cap. If a utility chooses not to adopt opportunity cost pricing, the non-firm rate is capped at the firm rate. We also wish to ensure that non-firm transmission service is priced in a nondiscriminatory fashion. Accordingly, if a transmission provider offers a rate discount to its affiliate, or if the transmission provider attributes a discounted rate to its own transactions, the same discounted rate must also be offered at the same time to non-affiliates on the same **[31,744]** transmission path and on all unconstrained transmission paths. We will further require that any affiliate discounts from the maximum firm rate must be transparent, readily understandable, and posted on the transmission provider's OASIS in advance so that all eligible customers have an equal opportunity to purchase non-firm transmission at the discounted rate.[454] In addition, discounts offered to non-affiliates must be on a basis that is not unduly discriminatory and must be reported on the OASIS within 24 hours of when

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[454]The same requirements will apply to discounts from firm transmission service. Similarly, if a transmission provider offers an affiliate a discount for ancillary services, or attributes a discounted ancillary service rate to its own transactions, it must offer at the same time the same discounted rate to all eligible customers. Discounted ancillary services rates must be posted on the OASIS pursuant to new Part 37 of the Commission's regulations.

available transmission capability (ATC) is adjusted in response to the transaction. As discussed in the RIN section, information, including the price for all non-firm transaction discounts, must be posted on the OASIS to ensure comparability.

2. Priority For Obtaining Service

The term "priority" is used in the comments in several senses. The intent of the comment depends on which kind of "priority" is intended. In general, there are comments about the order in which parties can obtain new service, which we call "reservation priority," and there are comments about the order in which parties lose service they already have, which we call "curtailment priority." Commenters may establish different reservation priorities for various services, such as network, off-system sales, firm, ability to reserve a portion of new transmission capacity to be constructed, and so on. Curtailment priorities also differ with the type of service. However, many commenters assert that certain parties should or should not have "priority" without distinguishing the kind of priority or type of service for which priority is intended.

a. Reservation Priority for Existing Firm Service Customers

Many IOUs, state commissions, and cooperatives strongly believe that native load should have priority to reserve transmission capacity under the tariffs.

EEI suggests that existing and future allocations of transmission capacity must be based on proper transmission pricing or, in its absence, priority of service. According to EEI, retail and existing wholesale requirements service should

have the highest priority for use of transmission capacity, followed by long-term point-to-point service. Dayton P&L supports a continued preference for native load growth because native load customers have borne the majority of the costs of the transmission system. Detroit Edison, EEI, and Florida Power Corp claim that, because native load and network customers pay higher rates during all hours, such customers should have higher priority for service requests than others requesting transmission service. These commenters also claim that the transmission provider should be able to reserve firm capacity for native load and network service customers.

Similarly, NARUC wants wholesale and retail native load customers to be held harmless from functional unbundling of wholesale transmission services. Because these customers have borne the vast majority of the costs of the utility's transmission facilities, NARUC argues that priority of service, quality of service, and allocation of joint and common costs to native load customers should not be affected by the transition to an open access transmission regime.

PA Com does not share the Commission's concern that a transmission provider may discriminate against a third party transmission customer vis-a-vis native load. It finds nothing impermissible in this sort of discrimination, arguing that the interconnected system was financed by, designed for, and built to serve native load.

NRECA explains that most transmission customers that seek network service will already be receiving similar service (albeit in a bundled form) from their transmission providers. It argues that these customers should receive the

same priority of service as the transmission provider's native load customers for as long as they continue to take network service, whether under a current bundled wholesale **[31,745]** supply contract, a private transmission contract, or a network tariff.[455]

East Kentucky requests that the final rule clarify that member distribution cooperatives of G&Ts will have priority over third parties in the use of the G&T's existing transmission facilities. TVA comments that native load customers and emergency service to neighboring systems should have a higher service priority than transmission services sold to third parties (where an alternative power supply is available to the third party).

Commission Conclusion

We reiterate that we are not requiring the transmission provider to unbundle transmission service to its retail native load nor are we requiring that bundled retail service be taken under the terms of the Final Rule pro forma tariff. However, the amount of transmission capacity available to wholesale and unbundled retail customers under the Final Rule pro forma tariff is clearly affected by the amount of transmission capacity that the transmission provider reserves for the use of its native load customers and the future load growth of those customers. The transmission provider may reserve in its calculation of ATC transmission capacity necessary to accommodate native load growth reasonably forecasted in its planning horizon. However, the transmission provider is

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[455]See also American Forest & Paper, AMP-Ohio.

obligated to provide transmission service to others under the Final Rule pro forma tariff out of capacity reserved for native load growth up to the time the capacity is actually needed for such future needs. Furthermore, as we explained previously, while existing wholesale customers do not have any ownership-like rights to the capacity they used during the term of their contract, they will have a right of first refusal to that capacity after the expiration of their contracts or when their contracts become subject to renewal or rollover.[456]

b. Reservation Priority for Firm Point-to-Point and Network Service

A number of commenters argue that all firm service should not be treated equally. These commenters argue that the price of the service should determine the priority that the service receives. A large number of IOUs and potential network customers (existing requirements customers) argue that in light of the pricing implicit in the NOPR, (i.e., 12 CP for network versus annual system peak for point-to-point) network service should have priority over point-to-point service (because, all other things being equal, the price for network service will be higher).

BG&E believes that a customer receiving service priority equal to native load and network customers should pay comparable rates. Thus, BG&E argues that either flexible firm point-to-point service should be priced the same as network service, or point-to-point service should have a lesser

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[456]See discussion in Section IV.A.5.

priority than native load and network service customers if point-to-point service is priced lower than network service.

DE Muni believes that native load and network customers must have priority access to interfaces (particularly where they are constrained) after system reliability concerns have been satisfied. The same argument is advanced by commenters concerning long-term service versus short-term service. Public Generating Pool argues that long-term service should always have priority over short-term service because long-term customers contribute more towards fixed-cost recovery than do short-term customers.

Cajun objects to having its service and service to its customers, which it characterizes as network service, receive the same priority as firm point-to-point service customers who take service for periods as short as one hour. Cajun points out that it, as well as other network and native load customers, have been paying and will be paying for the transmission facilities in place to serve their needs for many years. According to Cajun, the transient firm point-to-point customer should not have equal standing. Cajun suggests, however, that a long-term firm point-to-point customer taking service for ten years or more should have service priority equal to native load and network service customers.

SC Public Service Authority argues that the availability of short-term firm service with a priority equal to long-term service would provide a means for short-term **[31746]** customers to obtain the advantages of long-term firm service at a much lower total cost. As a result, it argues that a few point-to-point customers would opt for long-term firm

service, and the burden of the residual costs of the transmission system would fall on network customers.

EEI claims that priority for point-to-point service should be on a continuum of firmness, with reservation (as well as curtailment) priority based upon duration of service and specific negotiated terms. EEI proposes that the point-to-point tariff be modified to provide a first-tier category of flexible point-to- point transmission service that is comparable in priority, price, length, and terms of service to network service. EEI believes that this modification will resolve the problems that are associated with establishing priorities between network service and point-to-point service if the Commission retains different CP cost allocation methods for each service.

On the other hand, CCEM, a group of power marketers, supports the concept that all firm service should be treated equally, regardless of the term or the nature of service.

Commission Conclusion

An essential element of non-discriminatory transmission access is the right of transmission customers to reserve and purchase transmission service that is of the same quality as that used by the transmission provider in serving its wholesale requirements customers and retail load. Thus, we reject the proposal of some commenters that transmission providers need not provide firm point-to-point service that is of the same "firmness" as the transmission provider's service to native load. However, the fact that both network service and point-to-point service are provided on an equally firm

basis does not mean that both types of service must be priced or reserved in the same manner.

The comments about reservation priorities for firm services boil down to two concerns. First, due to the differences in pricing firm point-to-point service and network service implicit in the NOPR (i.e., twelve-monthly CP pricing for network versus annual system peak for point-to-point), some commenters believe that network service should have priority over point-to-point service. Second, some commenters maintain that according firm, short-term point-to-point service a priority equal to long-term service provides a means for short-term customers to avoid making a fair contribution to the long-term costs of the system.

With respect to the first concern, we have eliminated the differences in pricing by permitting utilities to adopt point-to-point reservations as the customer load. As discussed above, for purposes of the Final Rule pro forma tariff, utilities are free to propose a single cost allocation method for the two services.

The second area of concern arises because of the first-come first-served reservation priority in the NOPR point-to-point tariff. The Commission recognizes that the tariffs, as proposed in the NOPR, provide the opportunity for a customer to reserve certain valuable rights (e.g., the right to short-term firm service during peak periods) while avoiding in part the long-term costs of the system (perhaps by relying on non-firm service during lengthy off-peak periods when there is a substantially reduced chance of interruption). However, the Commission has a countervailing concern that the transmission provider should not be able to withhold

valuable transmission capacity from potential customers if that capacity is not being used by those who are paying for the long-term costs of the system.

Accordingly, the Final Rule pro forma tariff provides a mechanism to address this concern while safeguarding the rights of potential customers to obtain access to unused capacity. The tariff provides that reservations for short-term firm point-to-point service (less than one year) will be conditional until one day before the commencement of daily service, one week before the commencement of weekly service, and one month before the commencement of monthly service. These conditional reservations may be displaced by competing requests for longer-term firm point-to-point service. For example, a reservation for daily firm point-to-point service could be displaced by a request for weekly firm point-to-point service during an overlapping period. Before the applicable reservation deadline, a holder of a conditional firm point-to-point reservation would have the right of first refusal to match any longer-term firm point-to-point reservation before being displaced. After the deadline, the reservation becomes **[31,747]** unconditional, and the service would be entitled to the same priorities as any long-term point-to-point or network firm service.[457]

The Final Rule pro forma tariff does not propose point-to-point or network service with various degrees of firmness beyond the simple categories of firm and non-firm. When a customer requests firm transmission service,

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[457]The service itself, as opposed to reservations, is subject to the curtailment provisions discussed below.

reservation priorities are established based first on availability, and in the event the system is constrained, based on duration of the underlying firm service request; customers may choose the "firmness" of service they want by electing to take non-firm service, or by reserving and paying for firm service. We have not included any degrees of firmness in the Final Rule pro forma tariff because having intermediate categories of firmness under point-to-point or network service would, we believe, unnecessarily complicate the priority system. However, utilities are free to propose and fully support different reservation priority provisions for firm service in subsequent rate filings as long as those provisions are not unduly discriminatory, fully comply with the principles of comparability, and are priced appropriately.

c. Reservation Priorities for Non-Firm Service

IOUs, state commissions, and potential network customers tend to support the service reservation priorities for non-firm service set forth in the NOPR pro forma tariffs (i.e., transmission service by network customers for economy purchases to serve network load has a higher priority than non-firm point-to-point service, which has a higher priority than a firm point-to-point customer using transmission service at secondary points of receipt and delivery). However, because network customers pay a higher rate than point-to-point customers, these commenters argue that network customers should be permitted to use their off-peak load ratio share of the transmission system to make off-system sales. Many commenters argue that point-to-point customers can use their secondary service for both purchases and sales; thus, they believe it is discriminatory to limit network customers to purchases at secondary points.

Commenters that are opposed to the service reservation priority scheme in the NOPR pro forma tariffs argue that transmission providers will discriminate against third party users in favor of their native load economy purchases. These commenters argue that all non-firm service should have equal priority.

Other commenters, such as CINergy, would base priority on the duration of service. CINergy claims that this method would eliminate what it claims is an advantage (over network) given in the NOPR to point-to-point service in making short-term purchases. TVA notes that it establishes priority for non-firm service based on duration of service requested, with customers in each service category receiving priorities based on the rate they wish to pay.

Some commenters believe that the transmission price should affect the priority of customers to obtain non-firm transmission capacity.[458] However, other commenters argue that this seems to be precluded by the NOPR pro forma tariffs' service priority provisions.

Although PSE&G believes that the NOPR pro forma tariffs suggest a first-come, first-served allocation method for capacity in excess of that needed for firm transmission service, it proposes a fixed period of time for all potential users to submit bids for service (e.g., one week prior for monthly service), allowing the bid price to determine priority (i.e., the higher bid prices receive service priority over lower bid prices). According to PSE&G, customers could bid an "up

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[458] *E.g.*, Duke, Orange & Rockland.

to" rate subject to a price floor, with all revenues flowed back to firm service customers. TVA also advocates departing from the first-come, first-served approach for allocating some uses of the transmission system, claiming that price is an effective means to establish priority for non-firm and short-term firm services.

Utility Wind Interest Group requests that non-firm service used for transmitting renewable resources be given a higher priority than non-firm service used **[31,748]** for transmitting conventional resources because renewable resources cannot store their fuel supply. Commission Conclusion

We continue to believe that network economy purchases should have a reservation priority over non-firm point-to-point and secondary point-to-point uses of the transmission system. Network transmission customers are obliged to pay all of the costs of the transmission system without regard to the resources from which energy is scheduled. Therefore, it is appropriate that the transmission associated with a network customer's economy purchases (i.e., transmission that is used to substitute one resource for another on an as-available basis) enjoys a higher priority than non-firm point-to-point transmission service.

Regarding the reservation priority for non-firm service under point-to-point service, we will adopt a reservation priority based upon duration of non-firm service, with price acting as a tie-breaker for competing service requests of an equal duration. If there is insufficient transmission capacity to accommodate all non-firm transmission requests, the reservation of longer duration should displace the shorter. For

example, a reservation for a month of non-firm service will displace a reservation for a week of non-firm service. Also, a reservation for a week will displace a reservation for a day, which will displace a reservation for an hour of non-firm service. If a customer requests non-firm and later another customer requests longer-term non-firm service before either term of service begins, the first customer to request service has the right of first refusal to change its request to the longer term of service. A firm point-to-point customer's use of transmission service at secondary points of receipt and delivery will continue to have the lowest reservation priority.

3. Curtailment Provisions

a. Pro-Rata Curtailment Provisions

A large number of IOUs that are control area operators argue for discretion to curtail the transaction that most effectively relieves the constraint, in lieu of mandatory pro-rata curtailments, which they argue are inappropriate and not cost effective.

Other commenters that do not support pro-rata curtailment argue that preference should be given to native load or existing customers because these customers have paid the majority of the costs of the transmission system. A large number of customers note that their existing contracts contain "enhanced" curtailment priorities (i.e., service to others will be curtailed before service to customers with such curtailment

priority) due to the large capital outlays made by them in connection with their service.[459]

Public Generating Pool believes that the proposed curtailment provisions may not be flexible enough for transactions in the Northwest. It argues that hydro spill should be avoided, and suggests that transactions from federal and/or non-federal hydroelectric generation facilities should not be curtailed pro rata with other transactions that do not rely on such facilities. Public Generating Pool urges that regional agreements (e.g., regional transmission group agreements) that would achieve this goal should be given deference.

Other commenters support pro-rata curtailments for firm service.[460] PSNM states that this has been its operating practice in the past, and PSNM expects to continue such an approach in the future.

Power marketer commenters generally support the pro-rata curtailment adding that a standardized curtailment priority applied nationally would provide greater open access and eliminate discriminatory curtailments.

Commenting on a related subject, EEI maintains that the network tariff provision for termination of service in the event a customer fails to curtail load[461] may not be realistic for

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[459]*E.g.*, TANC, Turlock, SMUD.

[460]*E.g.*, PSNM and Nebraska Public Power District.

[461]Proposed Pro Forma Network tariff section 9.7 - System Reliability.

service to a Transmission Dependent Utility. EEI suggests that the Commission supplement this provision with a substantial penalty provision, coupled with an indemnification requirement.

[31,749]
Commission Conclusion

It was not our intent in the NOPR to require all transactions to be curtailed on a pro-rata basis regardless of whether the transaction relieves a constraint. We intended to permit curtailments of transactions that substantially relieve a constraint.[462] We intended and continue to believe that curtailment on a pro-rata basis is appropriate for curtailing the transactions that substantially relieve the constraint. In order to allay the concerns of the commenters addressing this issue,

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[462]The Final Rule pro forma tariff contains language allowing the transmission provider the discretion to interrupt firm transmission service in an emergency or other unforeseen condition in a manner suggested by these commenters. Section 11.6, Curtailment of Firm Service, of the Final Rule pro forma tariff provides:

However, the Transmission Provider reserves the right to interrupt, in whole or in part, firm Transmission Service provided under this Tariff when, in the Transmission Provider's sole discretion, an emergency or other unforeseen condition impairs or degrades the reliability of its transmission system.

The reference to curtailments being allocated on a proportional (pro rata) basis addresses situations where multiple transactions could be curtailed to relieve a constraint.

we are clarifying the curtailment provision of the tariff to explicitly allow the transmission provider discretion to curtail the services, whether firm or non-firm, that substantially relieve the constraint. Of course, any curtailment must be made on a non-discriminatory basis, including curtailment of the transmission provider's own use of the transmission system. Customers that believe the curtailment policy is administered unfairly may file a section 206 complaint at the Commission.

Concerning the request of certain Pacific Northwest commenters, we would consider granting deference to an alternative curtailment method to avoid hydro spill if such a regional practice is generally accepted and adhered to across the region, as discussed further in Section IV.K.

Finally, we agree with EEI's observation that terminating network service under the tariff to a transmission dependent utility that fails to curtail load as required may not be appropriate. As a result, we clarify that under network and point-to-point service, the transmission provider may propose a rate treatment (penalty provision) to apply in the event a customer fails to curtail load as required under the Final Rule pro forma tariff. Such proposals will be evaluated on a case-by-case basis on compliance.

b. Curtailment Provisions for Non-Firm Service

A number of commenters seek clarification of the curtailment provision for non-firm service under the two tariffs. They note that economy purchases by the network customer are accorded a higher curtailment priority than non-firm service under the point-to-point tariff. However, under

the point-to-point tariff there is no acknowledgement of this higher priority for network service. Curtailments for non-firm transmission service under the point-to-point tariff are simply based upon duration of service, without reference to a higher priority for network economy purchases.

A number of commenters, including Industrial Energy Applications, suggest that a price-based curtailment queue for non-firm transmission will facilitate economy energy deals in highly competitive wholesale power supply markets and allow the parties to directly address delivery risk through the pricing mechanism.

Blue Ridge argues that the final rule should provide equal curtailment priority for all types of non-firm transmission service. Utilities For Improved Transition argues that network customers should be able to transmit non-firm power imports under the network tariff with the same curtailment priority that is assigned to all other firm network uses of the transmission system.

A number of commenters note that the tariffs allow non-firm service to be interrupted only for emergency or reliability reasons or to provide firm service. These commenters contend that, under this requirement, curtailment of non-firm service is unlikely.[463] As a result, they believe that non-firm service is elevated to firm service. To remedy this situation, these commenters argue that transmission

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[463] *E.g.*, Florida Power & Light Company, Southern California Edison Company.

providers should have the ability to **[31,750]** curtail non-firm service for any economic reason.

Commission Conclusion

We have clarified in the Final Rule pro forma tariff that a network customer's economy purchases have a higher curtailment priority than non-firm point-to-point transmission service.

A higher curtailment priority should be provided to network economy energy purchases for the reasons stated in AES Power, Inc..[464] In that case, we recognized that the network transmission customer has already "paid" for the transmission of its economy purchases (i.e., transmission that is used to substitute one resource for another on an as available basis) through its payment of a load ratio share of the system.

Many commenters oppose the point-to-point service provision allowing non-firm service to be interrupted only for emergency or reliability reasons or to provide firm service. Upon further consideration, we agree that this provision is too narrow. Accordingly, the Final Rule pro forma tariff is revised to allow the transmission provider to curtail non-firm service for reliability reasons or economic reasons (i.e., in order to accommodate (1) a request for firm transmission service, (2) a request for non-firm service of greater duration, (3) a request for non-firm transmission service of equal

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[464]69 FERC ¶61,145 at p. 62,300 (1994) (proposed order), 74 FERC ¶61,220 (1996) (final order).

duration with a higher price, or (4) transmission service for economy purchases by network customers from non-designated resources.). However, all curtailments must continue to be made on a non-discriminatory basis including curtailments of the transmission provider's own non-firm uses of the transmission system under the tariff. A firm point-to-point customer's use of transmission service at secondary points of receipt and delivery will continue to have the lowest curtailment priority.

4. Specific Tariff Provisions

a. Network and Point-to-Point Customers' Uses of the System

Generally, transmission providers argue that the tariffs give too much flexibility to customers, while transmission customers argue that even more flexibility is required. The arguments are generally tied to pricing rather than technical problems with providing any level of service.

A common transmission provider argument is that the proposed firm point-to-point tariff provides a premium service comparable to network service, but at a lower rate. It has been suggested that either the flexibility to use non-firm service at secondary points of receipt and/or delivery at no additional charge under the point-to-point tariff be eliminated or that point-to-point customers should pay a premium price for such flexibility.[465] Transmission providers generally argue that flexible point-to-point service puts the transmission owner

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[465] *E.g.*, EEI, Utility Working Group, SoCal Edison.

and the network customer at a competitive disadvantage. They assert that the point-to-point customer is able to use non-firm transmission to reach secondary receipt and delivery points for both sales and purchases, but the network customer may use only non-firm transmission to reach secondary points for purchases. Thus, they argue, the flexible point-to-point users can sell non-firm power with a small or even no transmission component (because the underlying transmission is effectively free). Electric Consumers Alliance and Cajun believe that the owner and network customer competing for that sale should not be charged for the identical transaction. Absent a change to the point-to-point tariff, a number of transmission providers and state commissions (including Midwest Commissions) argue that to provide balance to the tariffs, the network tariff should permit the network customers to have non-firm transmission to secondary receipt and delivery points at no additional charge for both purchases and sales within its load-ratio transmission entitlement. Utilities For Improved Transition refers to this proposed network tariff modification as "headroom."

CCEM opposes the headroom concept, arguing that "free" use of capacity will give transmission providers an unfair competitive advantage. CCEM also cites Order No. 636 in support of its position.

Conversely, a number of customer groups believe the point-to-point tariff **[31,751]** should be made more flexible by broadly defining the concept of points of receipt and delivery. They argue that all points of connection between the transmitting utility and the purchasing utility should be treated as a single point of delivery (POD) or point of receipt

(POR).[466] In this manner, a customer would not have to pay for every point of receipt or point of delivery, but could select a contract demand level of service. The customer could then use the service at multiple points without incurring separate reservation charges for each point.

A number of commenters contend that the Commission should not force specific tariffs on public utilities in the Pacific Northwest due to their unique status.[467] In particular, NWRTA recommends that the final rule recognize that the Pacific Northwest's integrated transmission system, including large components owned by non-public utilities, was constructed to support a unique region-wide hydroelectric-dependent generating system. NWRTA recommends that the final rule be sufficiently flexible to accommodate these unique characteristics without prejudicing the interests of users or providers of transmission services.

Similarly, Public Generating Pool states that the NOPR pro forma network tariff departs from the status quo arrangements in the Northwest and is generally unworkable because generation is usually remote from the control area serving the network load and because BPA, which does not have a typical service territory, dominates the regional transmission market. Public Generating Pool suggests that the Commission require, and the region develop, a "generation integration" transmission tariff that would offer network-type

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[466] *E.g.*, Arkansas Cities, NRECA.

[467] *E.g.*, Public Power Council, Washington Water Power, NWRTA.

service to a source or sources of generation unbundled from the "network services" designed to integrate load. Similar contract demand network tariffs have already been proposed by some IOUs.

Commission Conclusion

We will not allow network customers to make off-system sales within the load-ratio transmission entitlement at no additional charge. Commenters have raised no new arguments to persuade us to do so, The primary purpose of network service is to integrate resources to serve loads. Use of transmission by network customers for non-firm economy purchases, which are used to displace firm network resources, must be accorded a higher priority than non-firm point-to-point service and secondary point-to-point service under the tariff. Off-system sales transactions. which are sales other than those to serve a network customer's native load, must be made using point-to-point service. They can be made on either a firm or non-firm basis.

A large number of transmission providers support the "headroom" concept, arguing that without it the flexible point-to-point service puts them at a competitive disadvantage. This would be true if a utility serving load were required to use network service exclusively, However, we do not require any utility to take network service to integrate resources and loads. If any transmission user (including the public utility) prefers to take flexible point-to-point service,[468] they are free to do so. Any point-to-point customer may take advantage of the secondary, non-firm flexibility provided under point-to-point service equally, on an as-available basis.

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[468] *See Florida Municipal Power Agency v. Florida Power & Light Company*, 74 FERC ¶61,006 at p. 61,013 and n. 70 (1996).

b. Minimum and Maximum Service Periods

Commenters raise issues regarding the minimum term of one hour for firm point-to-point service. Their concerns center on price and priority. Transmission providers point out that their native load customers pay the fixed cost of the transmission system every hour of the year. They argue that comparability is not achieved by permitting others to have service for one hour with equal priority to native load and other long-term customers. Others worry that the one-hour minimum term will: (1) Promote the selective use of the transmission system: (2) impair the ability of a utility to plan its system; and (3) adversely impact longer term transactions.

Tallahassee and KY Com are concerned that one-hour firm service may encourage **[31,752]** speculative advance requests for service during the system peak day (Cajun refers to this as cream skimming). These commenters express concern that such requests could displace other valid transactions or constrain a corridor or interface to the detriment of network service or native load customers, Tallahassee proposes a one-day minimum term for firm service.[469]

East Kentucky is concerned that users of the transmission system could, under the Commission's proposed open-access rule, purchase short-term firm service during peak months in lieu of annual firm service to reduce expenses associated with the purchase of firm transmission service. By buying short-term firm service only during the peak months,

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[469]See also VEPCO, CSW, NYSEG, WP&L.

an entity can significantly reduce its transmission expenses by purchasing non-firm service during off-peak months when the available transmission capacity far exceeds the demand on the transmission system. For this reason, some commenters request that short-term firm service be priced to generate revenues over the peak months equal to the charge for annual firm service.

Duke argues that, because all curtailments are equal, the addition of each one hour firm transaction will lower the reliability profile of native load customers and other customers with long-term commitments. It suggests that different classes of services be established that offer transmission customers the flexibility to obtain an intermediate level of transmission service (between native load firm and non-firm) for transactions of shorter duration.

On the other hand, some TDUs and power marketers support the one-hour minimum term. TAPS argues that transmission providers should not be permitted to restrict the availability of hourly, daily or weekly transmission service at reasonable prices, as some transmission providers have proposed in open access cases. Brazos supports a minimum duration of service equal to the minimum scheduling period of the transmission owner. Turning to the maximum term of service, Chugach objects to the imprecise requirement that transmission service be offered for a term equal to the life of a particular generation resource. Chugach, joined by VEPCO, suggests that the Commission require transmitting utilities to offer five-year terms (with longer contract terms by negotiated agreement).

Although BPA supports eliminating arbitrary term limitations and facilitating long-term resource commitments, it is concerned that the Commission's failure to specify a maximum term for firm transmission service (particularly where no specific resource is being wheeled) requires transmitting utilities to effectively sell off their transmission capacity to third parties. In BPA's view. such a requirement goes well beyond the intent of the Energy Policy Act.

PSE&G argues that the term limit for firm transmission service should be consistent with the transmission provider's planning horizon (e.g., for PSE&G, 10 years), which will ensure comparability of firm third party customers with native load. According to ConEd, failure to specify a maximum term for service creates uncertainty for planning purposes. PECO believes that utilities should have the right to limit the term of service to either: (1) The expected useful life of facilities used in providing service; or (2) the term of permits and land rights needed for those facilities.

Commission Conclusion

We will adopt a one-day minimum term for firm point-to-point service. The one-day minimum term for firm point-to-point service, along with modifications to the procedures for requesting firm point-to-point service, will moot a number of reliability concerns and allegations about possible "cream-skimming." As discussed supra, firm service requests with longer durations of service will have bumping rights over shorter term firm service requests. Also, the one day minimum will not disadvantage anyone because the transmission provider will be subject to the same one-day

term for its firm point-to-point uses of the transmission system. Because of the longer-term nature of network service, it will be subject to a one-year minimum term.

We will not specify a maximum term for either point-to-point or network transmission service. However, we recognize the concerns raised by commenters that a **[31,753]** commitment of uncertain duration makes planning difficult. Therefore, we will modify the tariff to require that an application for transmission service specify the length of service being requested. This will provide the transmission provider with the certainty it needs for planning, and the transmission customer with the flexibility to request the service it needs.

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[pp. 31,764 - 31,766]

[31,764]

(a) Transmission Provider's Use of Its System (Charging Yourself)

The purpose of functional unbundling is to separate the transmission component of all new transactions occurring under the Final Rule pro forma tariff, thereby assisting in the verification of a transmission provider's compliance with the comparability requirement. For example, if a transmission provider makes an off-system power sale, functional unbundling requires that the revenues received from that third-party customer be unbundled into specific transmission and production components. The transmission component of the revenues would be the product of the amount of

transmission capacity used in making the sale and the applicable rate. With respect to off-system sales, the transmission provider would book to operating revenue accounts those revenues received from the customer to whom it made the off-system sale. We will require that the transmission service component and energy component of those revenues be recorded in separate subaccounts of Account 447, Sales for Resale.

(b) Facilities and System Impact Studies

Comparability mandates that to the extent a transmission provider charges transmission customers for the costs of performing specific facilities or system impact studies related to a service request, the transmission provider also must separately record the costs associated with specific studies undertaken on behalf of its own native load customers, or, for example, for making an off-system sale. Utilities choosing this method of recovering the cost of specific studies must keep detailed expense records pertaining to each specific study. We will require utilities to record the cost of such studies that are properly includable in the determination of net income for the period in a separate subaccount of Account 566, Miscellaneous Transmission Expenses. We note, however, that not all studies performed by a transmission provider will benefit only a single customer. To the extent a transmission provider performs a system impact study that is useful in providing service to all transmission customers, the costs should be allocated to all customers.

(c) Ancillary Services

To ensure comparable transmission access a transmission provider is obligated to provide, or offer to provide, certain ancillary services to the transmission customer. Also, the transmission provider may offer to provide other ancillary services to the transmission customer, as discussed in Section IV.D. A transmission customer is obligated to purchase certain ancillary services from the transmission provider.

Generation resources provide certain ancillary services, while transmission resources provide other ancillary services. Consequently, the costs of providing certain ancillary services are recorded in the transmission provider's power production expense accounts,[504] while others are recorded in the transmission provider's transmission expense accounts.

Some commenters suggest that there may be a need for revising the Uniform System of Accounts to better track the **[31,765]** costs of providing discrete ancillary services. Other commenters believe that ancillary services are transmission-type services and suggested that the costs of generation-provided ancillary services be refunctionalized from power production expense to transmission expense.

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[504]This discussion applies to vertically integrated transmission providers. It may not apply, for example, to a transmission-only company or an independent system operator.

Currently, the Uniform System of Accounts requires that costs incurred in providing ancillary services are recorded as power production or transmission expense depending upon which resource the transmission provider uses to supply the service. At this time, we are not convinced that the amounts involved or the difficulty associated with measuring the cost of ancillary services warrants a departure from our present accounting requirements. However, in calculating separate rates for specific ancillary services utilities must maintain sufficient records and cost support for the derivation of the rates. Additionally, we will specify that the revenues a Transmission Provider receives from providing ancillary services must be recorded by type of service in Account 447, Sales for Resale, or Account 456, Other Electric Revenues, as appropriate.

(3) Liability and Indemnification

A number of commenters addressed the liability and indemnification provisions of the proposed pro forma tariffs. Duke argues that the proposed language confuses and conflates the limitation on the Transmission Provider's and Customer's rights against each other if a force majeure event occurs, and the requirement of indemnification against claims by third parties.

EEI argues that the proposed indemnification provision is inappropriate because it applies both ways, that is, the Transmission Provider and Customer indemnify each other against third party claims arising on their own systems. EEI suggests that the provision, as written, could result in the utility being required to indemnify the customer against damages incurred if, for example, an individual pried open a

transformer to steal materials and in the process was electrocuted. This concern was also voiced by Consolidated Edison, NYSEG, and Virginia Electric and Power Company. Consumer Power suggests that the best answer to this issue may be to leave the issue of allocation of risk to the contracting parties, to be resolved by negotiation when a Service Agreement is drawn up.

The Coalition for a Competitive Market, on the other hand, argues that the indemnification provision, as proposed, provides too much of a limitation of the Transmission Provider's liability, requiring gross negligence rather than simple negligence before the Transmission Provider can be held liable for damages to third parties arising from the Transmission Provider's actions.

Commission Conclusion

We agree with the commenters that these risk allocation provisions must be carefully drafted so that transmission providers and customers can accurately assess and account for their respective risks. The indemnification provision has now been broken into two parts. The first part is a force majeure provision which provides that neither the transmission provider nor the customer will be in default if a force majeure event occurs, but also provides that both the transmission provider and customer will take all reasonable steps to comply with the tariff despite the occurrence of a force majeure event. This protection against unexpected and unpredictable events is appropriately made available to both the transmission provider and transmission customer.

The second portion of the provision provides for indemnification against third party claims arising from the performance of obligations under the tariff. We have limited the indemnification portion of the provision so that it is now only the transmission customer who indemnifies the transmission provider from the claims of third parties. The customer is taking service from the transmission provider and may appropriately be asked to bear the risks of third-party suits arising from the provision of service to the customer under the tariff. We find that this new indemnification provision would be too strict if it required customers to indemnify transmission providers even in cases where the transmission provider is negligent. See Pacific Interstate Offshore Company, 62 FERC para. 61,260 at 62,733-34 (requiring amendment of indemnification provisions that required indemnification except in cases of "gross negligence"). Accordingly, the revised provision provides that the customer will not be required to **[31,766]** indemnify the transmission provider in the case of negligence or intentional wrongdoing by the transmission provider.

(4) Miscellaneous Clarifications

(a) Electronic Format

In the NOPR, we proposed that public utilities making Stage Two filings be required, in addition to the requirements specified in Part 35, to file copies of such filings on a diskette in ASCII format. We will now require that public utilities, in addition to complying with the requirements of Part 35, submit a complete electronic version of all transmission tariffs and service agreements in a word processor format, with the diskette labeled as to the format (including version) used,

initially and each time changes are filed. After the initial compliance filing, utilities proposing changes to the Final Rule pro forma tariff terms and conditions must provide a detailed list of changes and, to the extent practicable, provide an electronic version that reflects changes in redline/strikeout format.

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[pp. 31,770 - 31,785]

[31,770]

I. Federal and State Jurisdiction: Transmission/Local Distribution In the original Stranded Cost NOPR, the Commission clarified that it has exclusive jurisdiction over unbundled retail transmission in interstate commerce by public utilities: it found that the Commission has exclusive jurisdiction over the rates, terms, and conditions of unbundled retail transmission in interstate commerce by public utilities, up to the point of local distribution. In the Open Access NOPR, the Commission reaffirmed this jurisdictional determination[515] and also **[31,771]** addressed the distinction

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[515]That determination included the situation in which a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In that scenario, the Commission would have jurisdiction over all of the transmission facilities used for the unbundled wheeling provided by the intervening public utilities. The NOPR also noted that the Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would

between transmission and local distribution. The Commission stated three reasons for expressing its views on the distinction between Commission-jurisdictional transmission in interstate commerce and state-jurisdictional local distribution, in the context of unbundled retail wheeling by public utilities.[516] First, facilities that can be used for wholesale transmission in interstate commerce by a public utility would be subject to the Commission's open access requirements. Second, states have authority to address retail stranded costs and stranded benefits through their jurisdiction over facilities used in local distribution. Third, as the structure of the industry continues to change dramatically, utilities need to know which regulator has jurisdiction over which facilities and services in order to meet state and federal filing requirements. Accordingly, the NOPR set forth our jurisdictional analysis and several technical factors, for determining what constitutes "facilities used in local distribution."

For unbundled wholesale wheeling, the NOPR proposed to apply a functional test, i.e., whether the entity to whom the power is delivered is a lawful reseller. For unbundled retail wheeling, the NOPR proposed to apply a

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be a retail sale. *FERC Statutes and Regulations* ¶32,514 at p. 33,144.

[516]The term "wheeling" is intended to cover any delivery of electric energy from a supplier to a purchaser, i.e., transmission, distribution, and/or local distribution. The Commission also has jurisdiction to order wholesale transmission services in either interstate or intrastate commerce by transmitting utilities that are not also public utilities. *See Tex-La Electric Cooperative of Texas, Inc.*, 67 FERC ¶61,019 (1994), reh'g pending.

combination functional-technical test that would take into account technical characteristics of the facilities used for the wheeling. The Commission proposed seven indicators of local distribution to be evaluated on a case-by-case basis:

(1) Local distribution facilities are normally in close proximity to retail customers.

(2) Local distribution facilities are primarily radial in character.

(3) Power flows into local distribution systems; it rarely, if ever, flows out.

(4) When power enters a local distribution system, it is not reconsigned or transported on to some other market.

(5) Power entering a local distribution system is consumed in a comparatively restricted geographical area.

(6) Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

(7) Local distribution systems will be of reduced voltage.[517]

The NOPR concluded that the application of these tests will enable states to address stranded costs by imposing an exit fee on departing retail customers, or including an adder

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[517] *FERC Statutes and Regulations* ¶32,514 at p. 33,145.

in the retail customers' local distribution rates.[518] In the NOPR, the Commission also addressed buy-sell transactions in which an end user arranges for the purchase of generation from a third-party supplier and a public utility transmits that energy in interstate commerce and re-sells it as part of a "nominal" bundled retail sale to the end user. We explained that the retail sale is actually the functional equivalent of two unbundled sales (one transmission and the other the sale of power) and that we have exclusive jurisdiction over the voluntary sale by public utilities of unbundled transmission at retail in interstate commerce.[519]

Several commenters support the Commission's proposed jurisdictional demarcation.[520] **[31,772]** San Diego G&E states that the Commission correctly proposed to look at both functional factors (such as whether the service is retail or wholesale) and technical factors (such as voltage). PG&E states that the NOPR's functional/technical test is preferable to a bright line voltage test.

Consumers Power states that the Commission has exclusive jurisdiction over all wheeling on an interconnected interstate transmission grid. It suggests that the Commission and the states act through a joint board or hearing to resolve jurisdictional differences and develop a bright line test.

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[518]Id. at p. 33,144-45.

[519]As discussed infra, there also would be a component of local distribution in such a transaction that would be subject to state jurisdiction.

[520]*E.g.*, PG&E, Wisconsin Coalition, Com Ed.

PSE&G and PG&E express concern that if retail wheeling is implemented, there may be loopholes that would enable customers to evade state jurisdiction and thus avoid paying stranded costs. For example, PSE&G is concerned that a retail customer may request transmission service only and a state commission will be unable to attach a retail stranded cost surcharge to that customer. PG&E proposes adding another indicator to the functional/technical test -- a final tap to a retail customer -- to ensure that "high-voltage" retail customers do not evade the state's reach. Moreover, to ensure that retail customers cannot escape state jurisdiction, PG&E recommends that the Commission state, as a matter of policy, that "all retail customers taking retail transmission service from their host utility by definition take service over local distribution facilities."

CINergy agrees with the Commission that a distinction between transmission and local distribution is important, but emphasizes the practical need for clarity on a timely basis. To achieve certainty, CINergy proposes that the Commission allow public utilities to file, under section 205, classifications of their facilities as transmission or local distribution. CCEM endorses CINergy's proposal. Although NARUC disagrees that the Commission has jurisdiction over unbundled retail transmission, if the Commission reaffirms the NOPR regarding its jurisdiction, then NARUC supports CINergy's proposal.

PSE&G strongly supports the Commission's proposed case-by-case methodology for determining whether facilities should be classified as transmission or local distribution. SoCal Edison argues that since a utility may have difficulty determining which of its facilities are transmission and which

are local distribution, utilities and states should be able to ask the Commission to classify a particular facility. Portland and Orange & Rockland suggest that the Commission provide a forum to resolve disputes over the correct classification of particular facilities.

Ohio Edison states that the Commission should assume jurisdiction over unbundled retail transmission, but only where a state has required this unbundling. It also believes that the Commission should assert jurisdiction over the ancillary services necessary to provide this jurisdictional service.

NYSEG argues that the Commission lacks jurisdiction over the transmission component of bundled retail service. On the other hand, NYSEG argues that the statute, legislative history, and case law reveal that the Commission has jurisdiction over unbundled retail wheeling from source to load, since it is transmission in interstate commerce. NYSEG argues that the "local distribution" exception to the Commission's jurisdiction applies only to bundled sales of power at retail.

Several state commissions assert that states have rate authority over all facilities used to provide retail service.[521] IL Com argues that states have rate authority over all facilities used to provide retail service, regardless of whether the NOPR would classify these facilities as transmission or local distribution.

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[521] *E.g.*, NM Com, NC Com, AZ Com.

MI Com, citing Connecticut Light & Power Company v. Federal Power Commission, 324 U.S. 515 (1945) (CL&P), and Arkansas Electric Cooperative v. Arkansas Public Service Commission, 461 U.S. 375, 393-94 (1983), contends that states have plenary jurisdiction over all aspects of retail service, including retail access and unbundled retail transmission service. It asserts that the Commission's effort to expand federal jurisdiction into transmission in connection with retail sales is without statutory justification.

Legal Environmental Assistance argues that the NOPR creates confusion about, and may intrude onto, state jurisdiction. **[31,773]** NYMEX argues that when a state orders retail wheeling, the state should have jurisdiction over that transmission-only service.

Oklahoma G&E, citing CL&P and United States v. California Public Utilities Commission, 345 U.S. 295, 316 (1953), asserts that the Commission failed to explain that the term "transmission in interstate commerce" could have different meanings depending on the factual context in which the term is applied. It argues that "transmission in interstate commerce" means the movement, in bulk, of electric energy flowing in interstate commerce, as opposed to the movement of electric energy that has been subdivided for delivery to consumers.

Oklahoma G&E further argues that "[t]he distinction between interconnected operation and radial operation corresponds precisely to this distinction between activities that have potential interstate effects and those that might have interstate effects but are a matter of primarily local

concern."[522] Oklahoma G&E also disagrees that the transportation of electric energy sold at wholesale necessarily constitutes transmission in interstate commerce. It argues that the Commission has misapplied case precedent and, by focusing on the level of the associated power sale, the Commission has misunderstood what constitutes a functional distinction between transmission in interstate commerce and local distribution.

NY Com asserts that the grant of jurisdiction to the Commission over wholesale power transactions in interstate commerce under section 201 of the FPA does not reduce the states' authority over local distribution (citing CL&P and Federal Power Commission v. Florida Power & Light Company, 404 U.S. 453, 467 (1972)). NY Com argues that the NOPR's assertion of exclusive jurisdiction over all facilities used to deliver electricity for resale, even those traditionally regarded as local distribution, violates Congress' assignment of local electric distribution to the states. It takes issue with the Commission's list of factors and says that states and the Commission should agree on a definition that preserves the traditional classification of local distribution facilities. According to NY Com, such definition should focus on the functional characteristics of local electric systems -- i.e., electricity flows into a comparatively restricted geographic area and does not flow back out of that area, and the power is consumed in that area.

NY IOUs argue that the Commission has jurisdiction over unbundled, but not bundled retail wheeling. It says that

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[522]Oklahoma G&E Initial Comments at p. 16.

other factors, including the indicators listed in the NOPR, are irrelevant, and that even long-distance interstate transmission is under state jurisdiction as long as it is bundled with a retail sale. According to NY IOUs, this is the plain meaning of the FPA; resort to legislative history is unnecessary. NY IOUs bases this view on section 201(a), which says that federal regulation extends only to matters not subject to state regulation. NY IOUs says that the only matters subject to state regulation were bundled retail sales, and that since transmission was part of the bundle, Congress intended transmission to stay under state authority as long as it is part of that bundle. It also cites section 201(b), which sets forth exceptions from Commission jurisdiction, and section 201(c), which defines "transmission in interstate commerce" and thus also controls the definition of transmission in intrastate commerce. Finally, NY IOUs argues that the legislative history supports its view, as does the case law.

Central Louisiana believes that the costs of requiring a transmission provider to take unbundled transmission service for both wholesale and retail purposes would far exceed any benefits. In this regard, Central Louisiana says that states clearly have jurisdiction over bundled retail transmission charges and that the proposed approach could not be implemented without states giving up jurisdiction or the passage of new federal legislation.

MN DPS disagrees on legal and policy grounds with the Commission's assertion of jurisdiction over unbundled retail transmission services.[523] It maintains that the

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[523]See also OH Com.

Commission's arguments do not negate the language of the FPA specifying that regulation of retail sales of electric energy is reserved to the states. MN DPS argues that the Commission's arguments **[31,774]** in support of its position are not on point because the issue is state authority to set rates for retail sales, not interstate commerce. Further, it declares that jurisdiction over a service does not change simply because it is priced differently.

Several commenters argue that unbundled pricing should not expand the Commission's jurisdiction.[524] NARUC argues that the NOPR did not explain why the Commission's authority attaches only to unbundled retail transmission service, why unbundling is jurisdictionally significant, and how transmission of electricity to end users differs from unbundled interstate transmission of natural gas by local distribution companies, which is subject to state regulation. Thus, NARUC urges the Commission not to claim jurisdiction over unbundled retail transmission services.

NARUC also argues that the Commission's test for distinguishing between transmission and local distribution is not a bright line as discussed in Federal Power Commission v. Southern California Edison Company, 376 U.S. 205 (1964) (Colton). NARUC concludes that when a state determines to enable a retail customer to purchase power from a third-party provider, that state retains the authority to regulate the delivery service provided by the utility.

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[524] *E.g.*, DOD, NM Com, KY Com, ABATE.

IL Com asserts that the test should be whether the utility function over which the Commission seeks to exercise jurisdiction is one which falls within the Attleboro gap.[525] It argues that the Commission has no legal authority to prescribe conditions under which a public utility may provide transmission service within its own service territory to its own retail customers. IL Com concedes that the court cases cited by the Commission can be interpreted to support widely disparate legal and policy positions, but argues that those cases resolved questions of Commission jurisdiction in circumstances where wholesale sales of electric power were being examined and not circumstances where retail sales are being considered. It contends that the question of whether the Commission should exercise jurisdiction over all transmission in retail wheeling has never been addressed before and requires a careful examination of the underlying purposes of Congress in enacting the FPA. IL Com explains that transmission by an Illinois utility of power to a retail consumer within its own service territory is not subject to Commission jurisdiction because that transmission was never within the Attleboro gap and has always been regulated by states.

OK Com recommends that the Commission apply to the electric industry the same policy that it has adopted concerning its regulation of the gas industry and leave unbundled retail service regulation to state authorities.

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[525] *See Public Utilities Commission v. Attleboro Steam & Electric Company*, 273 U.S. 83 (1927).

WI Com argues that if a utility offers unbundled retail access, jurisdiction over transmission services should continue to be based upon the historical demarcation between wholesale and retail transactions. KY Com argues that Congress did not intend, by authorizing wholesale wheeling in the Energy Policy Act, to change the longstanding division of jurisdiction between the Commission and the states. It claims that the NOPR ignores the limitation in the FPA that the Commission has no jurisdiction over retail sales service. NV Com cites several cases noting the states' historical authority to regulate retail rates.

IA Com proposes a definition of local distribution and transmission that would preserve the jurisdictional status quo and does not put a state commission in the position of losing authority over certain elements of a retail transaction should it allow retail wheeling. IA Com's proposed definition is as follows:

Distribution -- Service provided by a utility directly connected to an ultimate consumer of electricity is a distribution service with respect to electric energy delivered to that consumer.

Transmission -- Service provided by a utility with respect to electric energy to be delivered to an ultimate consumer through another utility is a transmission service.[526] **[31,775]**

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[526]IA Com Initial Comments at p. 4.

Montana Power states that a reasonable way to give effect to the "local distribution" exemption is to define "local distribution" as a bundled retail sale, even if interstate facilities are used.

Several commenters criticized the NOPR's functional/physical indicators. PA Com disagrees with the Commission's discussion of the FPA's legislative history and asserts that the FPA does not address the issue of what constitutes local distribution. PA Com contends that the issue was resolved by the Supreme Court in CL&P in a manner contrary to the Commission's technical-functional test and that the NOPR minimized CL&P. NM Com asserts that the proposed engineering and functional elements for determining the status of local distribution facilities fail to account for the governmental or legalistic test requirement of the FPA as identified in CL&P.

KY Com concludes that a physical definition of distribution facilities, based on objective criteria, is consistent with the FPA and is necessary to provide a clean line of demarcation.

CO Com argues that Congress used a transactional test rather than a functional test and that Congress intended all retail transactions to be under state jurisdiction. According to CO Com, there is concurrent jurisdiction over unbundled transmission in interstate commerce to an end-user. Moreover, CO Com asserts that unbundled intrastate transmission to a wholesale purchaser is under state jurisdiction (citing section 201(b)(1)). Finally, CO Com argues that the state has authority over unbundled transmission in intrastate commerce to an end-user when the

transmission-providing utility, end-user, and generator are all within the same state.

Other commenters prefer a functional test. Natural Resources Defense, DOE, and Sustainable Energy Policy generally agree that a line needs to be drawn between transmission and local distribution but believe that the Commission's test is unnecessarily cumbersome or may lead to legal uncertainty, at least within the context of stranded benefits. Instead, Natural Resources Defense proposes the following functional test, which is based on end-use service:

The Federal Power Act does not affect state regulators' jurisdiction to apply distribution charges -- either volume-based or fixed -- to electricity that is used by any utility customer to provide end-use services (as distinguished from electricity that is purchased for resale to end-use customers).[527] Sustainable Energy Policy endorses Natural Resources Defense's position. DOE suggests that a functional definition of local distribution (i.e., electricity provided for end-use service) may be the best way to avoid legal uncertainty.

EPA argues that the Commission's proposed physical definition may encourage gaming to avoid stranded costs and costs associated with public policy goals such as energy efficiency, renewable energy development and R&D funding, and a physical definition assumes that power flows into, and not out of, distribution systems, which would not allow for distributed generation (e.g., fuel cells). Thus, EPA urges the

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[527]Natural Resources Defense Initial Comments at p. 3.

Commission to adopt a functional definition that "local distribution occurs whenever electricity is provided by a utility for end-use service." Alternatively, EPA suggests that the Commission add a provision to its approach that "the provision of electricity for end-use service generally involves local distribution." Sustainable Energy Policy suggests a non-bypassable charge levied on all users of the distribution system. It endorses the policy formulation set forth by Natural Resources Defense in its initial comments. Reynolds wants to ensure that there is always at least concurrent state jurisdiction over lines used to serve end-use customers, since only states can order retail wheeling.

Detroit Edison argues that state/federal jurisdictional issues should be resolved by focusing on the use of the facilities. It says that facilities that are used to distribute a utility's own power to its own local customers should be subject to state regulation, while the use of facilities for wholesale power transactions or wholesale or retail transmission in interstate commerce should be under federal regulation.

[31,776]

Mountain States Petroleum Assoc argues that the Commission should use a functional test based on state boundaries: if a line is in more than one state, there is Commission jurisdiction; if a line is entirely within one state, there is state jurisdiction.

MD Com states that it believes that the Commission's proposed indicators for determining where to draw the line are adequate, but adds that it does not concede the

Commission's assertion of jurisdiction over unbundled retail transmission.

Some commenters suggest that implementation of the NOPR's tests could have adverse consequences. NH Com objects to the NOPR's specific tests; for example, if the Commission asserts jurisdiction over facilities because they are not radial, New Hampshire's policy of encouraging looping rather than radial lines would have the ironic effect of destroying state jurisdiction. NJ BPU states that there may be situations when the NOPR factors would not produce the proper result. It requests that the final rule recognize the need for case-by-case flexibility in determining where federal jurisdiction ends, so that the Commission and the states can work cooperatively.

NRRI argues that the NOPR's test could make siting of new transmission lines more difficult because states have in the past required native load customers to pay that part of the transmission-related revenue requirement that is not covered by unbundled transmission service. NRRI contends that, if the Commission asserts jurisdiction over all unbundled transmission service and if there is a firm point-to-point service capacity right that has value and is reassignable, then state commissions might eliminate portions of the transmission systems subject to capacity rights from rate base. NRRI is also concerned that the NOPR's transmission/local distribution test could create a price squeeze between bundled and unbundled retail transmission rates.

IN Com argues that the NOPR's view of jurisdiction would discourage retail wheeling. It says that states will be reluctant to order wheeling if the result is that they lose

jurisdiction over the previously rolled-in transmission aspect of the service. It suggests that the Commission use negotiated rulemaking to address jurisdictional issues.

Several commenters suggest alternative approaches to jurisdictional line-drawing. NV Com suggests that the Commission consider federal and state jurisdiction over transmission by using "network" and "non-network" concepts:

> The "network" concept for regulation recognizes that there is an interstate network of electric facilities used to link generation with loads. The operation of that network is indifferent to whether the electrical flows are retail or wholesale flows. Conceptually, events on the network could fall under federal jurisdiction. Where facilities provide essential service for the delivery of power, but do not substantially affect the electrical flows on the network, the facilities fall outside the network and would remain within the traditional domain of the state commission. As a consequence the delineation of federal and state jurisdiction evolves from the recognition of the events and where they occur as opposed to a rigid consideration of the physical properties of the facilities involved.[528]

NV Com further explains that the determination of what is a network event would require a case-by-case examination.

OH Com asserts that Congress intends there to be a bright line between state and federal jurisdiction and that the Commission has failed to provide such a bright line. OH Com

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[528]NV Com Reply Comments at p. 3.

proposes the use of retail marketing areas to provide the bright line -- the jurisdictional line would be at the point at which power enters the retail marketing area of the entity delivering the power to the retail customer. OH Com cites section 212(g) of the FPA, as amended by the Energy Policy Act, which provides that the Commission cannot issue any order under the FPA inconsistent with state law governing retail marketing areas.

Under OH Com's proposal, the Commission would have jurisdiction over the wheeling-out and wheeling-through components of retail wheeling and the state would have jurisdiction over the wheeling-in component due to its local nature. OH Com concludes that the Commission's approach "fails to meet the legal standard **[31,777]** FERC must consider, and is inconsistent with the 'savings clause' and legitimacy of 'retail marketing areas' as discussed in the amended FPA."[529] OH Com also explains that the Commission's approach "is wreaking havoc on the state's ability to develop an interruptible buy-through arrangement to provide an increased competitive option for its retail customers."[530] OH Com further encourages the use of mutual

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[529]Sections 212(g) and 212(h) of the FPA.

[530]We note that since OH Com filed its comments, it approved an interruptible buy-through plan. *See Interruptible Electric Service Guidelines*, Case No. 95-866-EL-UNC, --PUR 4th-- (Ohio PUC Feb. 15, 1996). *See also Central Illinois Light Company*, Docket No. ER96-1075-000 (1996) (accepting amendment to open access transmission tariffs that expands service eligibility to accommodate participation in experimental retail wheeling pilot program approved by the Illinois Commerce

deference to promote Congress' intent in mandating a system of federal/state cooperation. In support, OH Com cites federal and state enforcement of telecommunications laws. NRRI also suggests that the jurisdictional line be drawn at the retail marketing area.

DC Com argues that the NOPR test is too difficult to administer and will create problems in determining the rate base at the state level. It suggests that the Commission should have jurisdiction over transmission from the source to the boundary of the "home" utility that delivers the power to the customer, with state jurisdiction over all aspects of the transmission service within that utility's franchise territory. AZ Com also expresses doubts that the NOPR's test is workable.

Several commenters propose that the Commission and state authorities address the jurisdictional issue jointly. SBA characterizes the Commission's proposed demarcation line as "laudable but misguided."[531] SBA recommends that a federal/state board be established to resolve the transmission/local distribution dilemma, similar to what

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Commission); *Illinois Power Company*, Docket No. ER96-1285-000, 75 FERC (1996); *cf. Illinois Power Company*, --PUR4th--, No. 95-0494 (Illinois Commerce Commission Mar. 13, 1996) (offering retail direct access service providing transmission and ancillary services using the rates, terms, and conditions of Illinois Power's open access tariff on file with the Commission); recently introduced legislation in Rhode Island, H.B. 8124, the Utility Restructuring Act of 1996.

[531]SBA Initial Comments at p. 36.

Congress did for allocating costs between interstate and intrastate communications. SBA explains that the problem in the communications industry was the impossibility of allocating a portion of a single copper wire to interstate or intrastate service.

AZ Com notes that even if the Commission is correct, the FPA clearly does not preempt a state from concluding that retail transmission or other direct access programs should be implemented in that state. AZ Com suggests that there may be concurrent jurisdiction and that mutually agreed-upon principles should be implemented to determine which jurisdiction should be given deference.

MD Com states that in determining the status of particular facilities, the Commission should give substantial weight to determinations made by states. ABATE states that the Commission could initially defer to states with respect to the determination of rates, terms, and conditions, while maintaining the right to review and overturn the state determination.

If the Commission maintains its position concerning jurisdiction, NARUC argues that the Commission should not implement its multi-factor test, but should enter into discussions with state commissions to develop workable alternatives. NH Com argues that pricing the retail part of a transaction, even if it involves use of the transmission system, should be subject only to state jurisdiction. NH Com wants to create a mechanism by which state and federal regulators combine their efforts in cooperative regulation; it suggests several alternatives such as state/federal agreements for shared jurisdiction.

KY Com and NRRI object to the statement in the NOPR that retail buy-through service is really transmission service (subject to the Commission's jurisdiction) plus a sale of generation at retail (subject to state jurisdiction). From a policy standpoint, KY Com argues that the Commission's approach creates a powerful disincentive for a state to embark on changes that otherwise might foster a more competitive environment. NRRI argues **[31,778]** that the Commission's approach may violate sections 212(g) and 212(h).

IL Com is concerned that industrial customers who get direct access may attempt to evade state jurisdiction, and thus avoid retail stranded cost charges, by bypassing facilities such as radial lines. It contends that retail wheeling rate surcharges would be a more effective means of recovering retail stranded costs if states were allowed to apply them to unbundled transmission and local distribution rates, not just the local distribution component of such rates.

NC Com asserts that "[a] significant cottage industry may well arise solely to convert retail customers into wholesale customers, thereby subverting the intent of Congress as expressly set forth in EPACT."[532] If the Commission does not adopt NARUC's proposal, NARUC asserts that the Commission's functional test should not permit an end user to bypass the distribution service provided by the utility. It urges the Commission to assure that there will be some facility involved in the transaction that will be defined as providing a local distribution service.

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[532]NC Com Initial Comments at p. 7.

NARUC also requests that the following sentence be added to proposed 18 CFR 35.27:

Nothing in this part limits the authority of a State commission in accordance with State law (1) to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission's jurisdiction, (2) to establish competitive procedures for the acquisition of such electric energy, or (3) to establish non-discriminatory fees for the delivery of such electric energy to retail consumers for purposes established in accordance with State law.([533])

Duke is concerned about the potential for regulatory gaps, which could lead to costs not being recovered from either federal or state jurisdiction. Duke is also concerned that where facilities are used for both wholesale and retail transactions, costs might not be recovered if federal and state regulators use different methods of cost allocation.

In response to the NOPR's proposal for functional unbundling,[534] CA Com agrees that it is important to draw a distinction between transmission and local distribution and that a bright line is not possible, but suggests that corporate or functional unbundling might provide a means to establish a workable bright line without relying on the more qualitative approach proposed in the NOPR. Arizona argues that rather than unbundling transmission for retail purposes, each utility

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[533]NARUC Reply Comments at p. 15-16.

[534]*FERC Statutes and Regulations* ¶32,514 at p. 33,080-83.

should establish a distribution function that would obtain transmission on behalf of retail customers, taking service under the utility's tariff. Arizona states that this would simplify the allocation of transmission costs, since all transmission costs would be under the Commission's jurisdiction. Arizona argues that the Commission should permit the utility to recover the distribution rate approved by the state. According to Arizona, this would create a bright line between state and federal jurisdiction.

TX Com argues that the proposed test would not be applicable to intrastate utilities in Texas because they do not operate in interstate commerce. Thus, it asserts that it should continue to regulate Electric Reliability Council of Texas (ERCOT) transmission and distribution service and deal with stranded cost issues that arise in connection with any retail wheeling initiatives.

Several commenters object to the Commission's proposal to assert jurisdiction over transactions that are buy-sell transactions in name only.[535] AEP argues that the Commission should avoid an unnecessary conflict over state/federal jurisdiction that may be caused by the NOPR's statement that buy-sell transactions are in fact transmission subject to Commission jurisdiction. It suggests that the Commission attempt to reach agreement with the states on this matter or ask Congress for any necessary statutory change. Citizens Utilities also argues that the Commission should not unbundle the interstate transmission aspect of buy-sell transactions. It says that, unlike the analogous **[31,779]** gas

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[535]See id. at p. 33,082.

contracts, buy-sell arrangements on the electric side are not an end run around clear federal jurisdiction. Further, it argues that it would be very difficult to define those buy-sell transactions that truly belong under federal jurisdiction.

IL Com also objects to the NOPR's characterization of buy-sell transactions. It argues that the fact that a transaction becomes unbundled does not suddenly make part of it under federal jurisdiction. Nucor argues that there is no need for the Commission to resolve this issue now; it suggests that the buy-sell arrangement is only tangentially related to open access. It argues that each buy-sell transaction will have to be addressed individually.

UT Com seeks clarification as to what the Commission means by buy-sell arrangements:

we currently authorize interruptible "buy-through" contracts, through which a retail customer, taking service subject to interruption for either economic or technical reasons, can opt to "buy-through" an interruption. The public utility purchases energy on behalf of the customer and sells it at cost to the customer. In our opinion, such transactions are not an example of a buy-sell transaction within the meaning of the proposed rule.[536]

DOD objects to the statement in the NOPR that "buy-sell" transactions are not really bundled retail service. It says that this view will discourage the development of innovative state programs, such as direct access programs. NYSEG also

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[536]UT Com Initial Comments at p. 4-5.

argues that buy-sell transactions are not under the Commission's jurisdiction. It argues that these transactions are unlike buy-sell transactions on the gas side, where the Commission asserted jurisdiction to prevent LDCs from circumventing the nondiscrimination standard it imposed on the release of capacity. NYSEG says:

> In contrast to its regulation of gas buy-sells, if the Commission regulates electric buy-sell transactions it would forego regulation of a transaction in which the Commission has a significant interest (i.e., access to the upstream seller's transmission), to regulate a transaction in which the Commission has virtually no interest (i.e., access to the distributing utility's system). Electric utilities must serve each retail customer irrespective of whether the customer takes traditional bundled service or retail buy-sell service. Unlike excess upstream gas pipeline capacity, the capacity on the local utility's electric system would not be allocated to another customer in a FERC jurisdictional transaction absent the electric buy-sell transaction. Electric buy-sell transactions are not designed so as to manipulate the assignment of upstream transmission capacity. Consequently, the impetus for FERC to reclassify gas buy-sell transactions as capacity assignments is not present in the electric context.[537]

NYSEG argues that there are only two possible grounds for the Commission's assertion of jurisdiction over electric buy-sell transactions: either (1) the sale for resale by the supplier is really a sale at retail to the end user, and the resale by the local utility is really unbundled retail wheeling;

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[537]NYSEG Initial Comments at p. 48 (footnote omitted).

or (2) the Commission has jurisdiction over transmission service that is part of bundled retail service. It claims that the second ground is invalid because the transmission aspect of bundled retail service is distribution. It also claims that the first ground is invalid because it assumes that the sale by the supplier to the local utility is not a sale for resale even though the contract says that it is. NYSEG states:

> The logical outcome would be that FERC would not have jurisdiction over the sale by the supplier to the utility, including transmission by that supplier because it would be a bundled retail sale. This is because, if the commission holds the resale to be a retail wheel, then it would have to find that the sale by the supplier is a retail sale to the end user. The Commission cannot at once regulate the sale for resale and the "retail transmission service." The Commission would regulate the transmission rates of the local franchise utility, although it would not regulate the access to such transmission service -- a matter FERC leaves to state regulators. In the process, FERC **[31,780]** would abandon the ability to regulate access to the supplier's bundled "retail power sale and transmission service," a transaction that FERC arguably has an interest in regulating.[538]

Finally, NYSEG argues that if the Commission insists on asserting jurisdiction, it should at least grandfather existing contracts.

UT Industrials state that where there is a state barrier to a buy-sell transaction, the Commission should allow the

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[538]NYSEG Initial Comments at p. 50.

utility to file a tariff with the Commission that would permit the utility to complete a voluntary buy-sell transaction as the NOPR proposes. However, it contends that when a state regulatory authority is authorized to, and has approved buy-sell transactions, it is not necessary for the Commission to become involved. It urges the Commission to allow such transactions to take place free of Commission regulation.
Commission Conclusion

In the discussion below, the Commission addresses the following jurisdictional issues raised in the prior NOPRs:

a. Does the Commission have jurisdiction over unbundled transmission in interstate commerce by a public utility when such transmission is used to transport electric energy that is sold to an end user?

b. If so, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

c. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

d. What procedures are appropriate for making jurisdictional determinations?

In addition, the Commission addresses concerns raised by state regulators which indicate that competition and open

access are perceived as threatening the traditional regulatory functions of state commissions. The Federal Power Act differentiates between state and federal regulation of electric power. As we discuss below, the Commission believes that any change in state or federal jurisdiction over physical transmission assets and related costs will not affect the traditional tasks of state and federal regulators.

The wide range of jurisdictional interpretations and proposals in the comments reflects the fact that the legislative history of the FPA and case law interpreting federal/state jurisdiction under that Act and the Natural Gas Act grew out of a market structure in which electricity and transmission generally were bought and sold on a bundled basis. As a result, most transactions included either a retail or wholesale sale of electric energy and jurisdictional lines were drawn on the basis of this sale. Thus, the cases simply do not resolve dispositively these jurisdictional issues when they arise in the context of the market structures and unbundled transactions being contemplated in today's electric industry. However, after reviewing the extensive analysis of the FPA, legislative history, and case law contained in both our initial Stranded Cost NOPR and in our Open Access NOPR, and the comments received on that analysis, we continue to believe that we were correct in asserting jurisdiction over the transmission component of an unbundled interstate retail wheeling transaction. We therefore reaffirm our conclusion. We also reaffirm and clarify our determinations regarding the tests to be used to determine what constitute Commission-jurisdictional transmission facilities and what constitute state-jurisdictional local distribution facilities in situations involving

unbundled wholesale wheeling and unbundled retail wheeling.[539]

At the same time, the Commission strongly supports the efforts of states to pursue pro-competitive policies. We recognize that jurisdictional issues raise overlapping Federal and state policy concerns that call for heightened cooperation among federal and state regulators. As discussed below, where states unbundle **[31,781]** retail sales, we will give deference to their determinations as to which facilities are transmission and which are local distribution, provided that the states, in making such determinations, apply the seven criteria discussed in the NOPR and reaffirmed below. In addition, we clarify our view that there is an element of local distribution service in any unbundled retail transaction, and further clarify other aspects of our jurisdictional ruling to preserve state jurisdiction over matters that are of local concern and will remain subject to state jurisdiction if retail unbundling occurs.

We first address our legal determination that if unbundled retail transmission in interstate commerce occurs voluntarily by a public utility or as a result of a state retail access program, this Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission. No commenter has raised cases or legislative history not previously considered in our prior NOPRs, and we will not

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[539]Not only do we conclude that our determinations are legally supportable under the case law, but we believe it is imperative to provide guidance to public utilities and state regulators as to our position on where the jurisdictional boundaries lie.

repeat here our full legal analysis of this issue.[540] However, we find compelling the fact that section 201 of the FPA, on its face, gives the Commission jurisdiction over transmission in interstate commerce (by public utilities) without qualification.[541] Unlike our jurisdiction over sales of electric energy, which section 201 of the FPA specifically limits to sales at wholesale, the statute does not limit our transmission jurisdiction over public utilities to wholesale transmission.

In response to those commenters (including NARUC) who argue that the Commission did not explain why its authority attaches only to unbundled, but not bundled, retail transmission in interstate commerce by public utilities, we believe that when transmission is sold at retail as part and parcel of the delivered product called electric energy, the transaction is a sale of electric energy at retail. Under the FPA, the Commission's jurisdiction over sales of electric energy extends only to wholesale sales. However, when a retail transaction is broken into two products that are sold

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[540]The Commission's complete legal analysis on this issue, and on the related issue of what facilities are Commission-jurisdictional transmission facilities, and what are state jurisdictional local distribution facilities, are contained in Appendix G to this Rule.

[541]Section 201(b)(1) specifically exempts from Commission jurisdiction facilities used for transmission in intrastate commerce and transmission of electric energy consumed wholly by the transmitter. As a result, we have no jurisdiction over retail wheeling that occurs in Alaska, Hawaii and the Electric Reliability Council (ERCOT) portion of Texas since transactions in those areas are intrastate.

separately (perhaps by two different suppliers: an electric energy supplier and a transmission supplier), we believe the jurisdictional lines change. In this situation, the state clearly retains jurisdiction over the sale of the power. However, the unbundled transmission service involves only the provision of "transmission in interstate commerce" which, under the FPA, is exclusively within the jurisdiction of the Commission. Therefore, when a bundled retail sale is unbundled and becomes separate transmission and power sales transactions, the resulting transmission transaction falls within the Federal sphere of regulation.

In asserting jurisdiction over unbundled retail transmission in interstate commerce by public utilities, the Commission in no way is asserting jurisdiction to order retail transmission directly to an ultimate consumer. Section 212(h) of the FPA clearly prohibits us from doing so. In addition, as stated in both the initial Stranded Cost NOPR and the Open Access NOPR, we do not address whether states have authority to order retail wheeling in interstate commerce. The Commission's assertion of jurisdiction is that if retail transmission in interstate commerce by a public utility occurs voluntarily or as a result of a state retail wheeling program, the Commission has exclusive jurisdiction over the rates, terms, and conditions of such transmission and public utilities offering such transmission must comply with the FPA by filing proposed rate schedules under section 205.

The Commission clarifies that nothing in this jurisdictional determination changes historical state franchise areas or interferes with state laws governing retail marketing areas of electric utilities. Section 212(g) of the FPA prohibits Commission orders that would be inconsistent with such laws.

However, we reject arguments made by some of the commenters **[31,782]** that section 212(g) could somehow be construed to give states authority over the rates, terms, and conditions of unbundled interstate transmission within retail marketing areas.[542] While our jurisdiction cannot affect whether and to whom a retail electric service territory (marketing area) is to be granted by the state, and whether such grant is exclusive or non-exclusive, neither can state jurisdiction affect this Commission's exclusivejurisdiction over transmission in interstate commerce by public utilities.

In response to several of the commenters, we further clarify that the Commission's jurisdiction over the rates, terms, and conditions of unbundled retail transmission is no broader than our authority over transmission used for wholesale transactions, and will not affect matters otherwise

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[542]The legislative history of FPA section 212(g) and its predecessor, former section 211(c)(3), indicates that the provision was focused on not interfering with state laws governing retail service territories and not permitting Commission wheeling orders "for purposes of sale by a utility to an ultimate consumer who is within the service territory of another utility (other than the applicant) where such territory is established by or under State law, rule, or decision." See H.R. Conf. Rep. No. 1750, 95th Cong., 2d Sess. 92 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 7797, 7826. Nothing on the face of section 212(g) or the legislative history of either the Energy Policy Act or PURPA indicates that the provision in any way affects the Commission's authority over rates, terms, and conditions of transmission in interstate commerce by public utilities.

left to the states by Congress.[543] The Federal Power Act recognizes that retail marketing areas are governed by state law. Moreover, we believe that states have authority over the service of delivering electric energy to end users. In exercising this authority, state regulatory commissions and state legislatures have traditionally developed social and environmental programs suited to the circumstances of their states. State regulation of most power production and virtually all distribution and consumption of electric energy is clearly distinguishable from this Commission's responsibility to ensure open and non-discriminatory interstate transmission service. Nothing adopted by the Commission today, including its interpretation of its authority over retail transmission or how the separate distribution and transmission functions and assets are discerned when retail service is unbundled, is inconsistent with traditional state regulatory authority in this area.

The Commission reiterates its strong interest in preventing any balkanization of the interstate power market. Although the Commission believes its Final Rule will accommodate retail competition, if it is offered voluntarily by a utility or ordered by a state, our policies relate only to the bulk power market and not traditional state regulation of the retail market.[544]

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[543]Among other things, Congress left to the States authority to regulate generation and transmission siting. See FPA sections 201(b) and 211(d)(1); Section 731 of the Energy Policy Act.

[544]This Final Rule will not affect or encroach upon state authority in such traditional areas as the authority over local service issues, including reliability of local service; administration of

NARUC has requested that the Commission specifically clarify in §35.27 of its proposed rules[545] that nothing in our final rule limits the authority of a state commission "to allow or disallow the inclusion of the costs of electric energy purchased at wholesale in retail rates subject to such State commission jurisdiction." We will adopt NARUC's proposal with modification, but add it as a separate subsection. The Final Rule adopts a new §35.27(b) as follows:

Nothing in this part (i) shall be construed as preempting or affecting any jurisdiction a state commission or other state authority mayhave under applicable state and federal law, or (ii) limits the authority of a state commission in accordance with state and federal law to establish (a) competitive procedures for the **[31,783]** acquisition of electric energy, including demand-side management, purchased at wholesale, or (b) non-discriminatory fees for the distribution of such electric energy to retail consumers for purposes established in accordance with state law.

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integrated resource planning and utility buy-side and demand-side decisions, including DSM; authority over utility generation and resource portfolios; and authority to impose non-bypassable distribution or retail stranded cost charges.

[545]Section 35.27 of the proposed rules provided that any public utility seeking authorization to engage in sales for resale at market-based rates shall not be required to demonstrate any lack of market power in generation with respect to sales from capacity first placed in service on or after 30 days from the date of publication of the Final Rule in the Federal Register. *FERC Statutes and Regulations* ¶32,514 at p. 33,154.

With respect to the Commission's adoption of the Open Access NOPR's functional/technical tests for determining what facilities are Commission-jurisdictional facilities used for transmission in interstate commerce and what facilities are state-jurisdictional local distribution facilities, the case law supports a bright line for unbundled wholesale transmission, i.e., transmission of electric energy that is being sold for resale. This is consistent with the bright line drawn by Congress to fill the Attleboro gap for regulating wholesale sales of electric energy. The case law also supports a bright line with respect to retail transmission by intervening utilities, i.e., transmission by those utilities between the new retail generation supplier and the public utility that previously provided bundled retail service to the end user. However, despite many commenters' arguments to the contrary, we cannot divine such a bright line for unbundled retail transmission by the public utility that previously provided bundled retail service to the end user. In fact, the limited case law, including CL&P and Colton, supports a case-by-case determination.[546] Accordingly, we believe our technical test, with its seven indicators, will permit reasoned factual determinations in individual cases.

Although we are unable to draw the bright line for local distribution facilities that many commenters would like, we believe it is important to make two clarifications regarding local distribution in the context of retail wheeling. First, even

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[546]As noted, the Commission's detailed legal analysis is contained in Appendix G. We are particularly persuaded by the Supreme Court's statement that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. See CL&P, 515 U.S. at p. 534-35.

when our technical test for local distribution facilities identifies no local distribution facilities for a specific transaction, we believe that states have authority over the service of delivering electric energy to end users. Second, through their jurisdiction over retail delivery services, states have authority not only to assess stranded costs but also to assess charges for stranded benefits, such as low-income assistance and demand-side management. Because their authority is over services, not just the facilities, states can assign stranded costs and benefits based on usage (kWh), demand (kW), or any combination or method they find appropriate. They do not have to assign them to specific facilities.[547]

Thus, while we believe in most cases there will be identifiable local distribution facilities subject to state jurisdiction, we also believe that even where there are no identifiable local distribution facilities, states nevertheless have jurisdiction in all circumstances over the service of delivering energy to end users. Under this interpretation of state/federal jurisdiction, customers have no incentive to structure a purchase so as to avoid using identifiable local distribution facilities in order to bypass state jurisdiction and thus avoid being assessed charges for stranded costs and benefits.

Based on concerns raised by state commissions as well as some utilities, we have further determined that it is

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[547]As noted above, states retain authority over state integrated resource planning, utility resource portfolios, and utility buy-side and demand-side decisions.

appropriate to provide deference to state commission recommendations regarding certain transmission/local distribution matters that arise when retail wheeling occurs. We also believe it is important to develop mechanisms to avoid regulatory conflict and to help provide certainty to utilities as to which regulator has jurisdiction over which facilities. These are discussed below.

Determining where to draw the jurisdictional line for facilities used in unbundled retail wheeling transactions will involve case-specific determinations that evaluate the seven local distribution indicators that we are adopting. We believe that the Commission should take advantage of state regulatory authorities' knowledge and expertise concerning the facilities of the utilities that they regulate. Therefore, in instances of unbundled retail wheeling that occurs as a result of a **[31,784]** state retail access program, we will defer to recommendations by state regulatory authorities concerning where to draw the jurisdictional line under the Commission's technical test for local distribution facilities, and how to allocate costs for such facilities to be included in rates, provided that such recommendations are consistent with the essential elements of the Final Rule.[548] Moreover, we recognize that in some cases the Commission's seven technical factors may not be fully dispositive and that states may find other technical factors that may be relevant. We will consider jurisdictional recommendations by states that take into account other

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[548]In order to give such deference, we expect state regulators to specifically evaluate the seven indicators and any other relevant facts and to make recommendations consistent with the essential elements of the Rule.

technical factors that the state believes are appropriate in light of historical uses of particular facilities.

Some commenters have asked the Commission to provide a forum to prevent or resolve disputes over the correct classification of facilities as transmission or local distribution. As a means of facilitating jurisdictional line-drawing, we will entertain proposals by public utilities, filed under section 205 of the FPA, containing classifications and/or cost allocations for transmission and local distribution facilities. However, as a prerequisite to filing transmission/local distribution facility classifications and/or cost allocations with the Commission, utilities must consult with their state regulatory authorities. If the utility's classifications and/or cost allocations are supported by the state regulatory authorities and are consistent with the principles established in the Final Rule, the Commission will defer to such classifications and/or cost allocations.[549] We encourage public utilities and their state regulatory authorities to attempt to agree to utility-specific classifications and allocations that the utility may file at the Commission.

A number of commenters have asked the Commission to defer to state commission recommendations or decisions regarding rates, terms and conditions of unbundled retail transmission in interstate commerce by public utilities. Some have suggested that we set broad guidelines for such rates, terms, and conditions, and then allow states to actually

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[549]This should also alleviate some concerns about the potential for costs not being accounted for if the Commission and a state commission use different methods of allocating costs.

implement the guidelines. While the Commission cannot simply turn over its jurisdiction for the states to implement, we understand the concerns raised by many state regulators and believe that deference to state commissions with regard to rates, terms, and conditions may be appropriate in some circumstances, as discussed below.

As we determined in the NOPR, when unbundled retail wheeling in interstate commerce occurs, the transaction has two components for jurisdictional purposes -- a transmission component and a local distribution component. The Commission has jurisdiction over facilities used for the transmission component of the transaction, and the state has jurisdiction over facilities used for the local distribution component.[550] Thus, the rates, terms and conditions of unbundled retail transmission by a public utility must be filed at the Commission. When this occurs, we will generally expect unbundled retail wheeling customers to take service under the same FERC tariff that applies to wholesale customers. However, if the unbundled retail wheeling occurs as part of a state retail access program, it may be appropriate to have a separate retail transmission tariff[551] to accommodate the design and special needs of such programs. In such situations, the Commission will defer to state requests for

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[550]As discussed above, even if there were instances where no local distribution facilities are used, we believe states have authority over the service of delivering electric energy to end users.

[551]*I.e.*, the tariff would be different from the tariff that applies to wholesale customers. Such tariff would still be filed with the Commission under FPA section 205.

variations from the FERC wholesale tariff to meet these local concerns, so long as the separate retail tariff is consistent with the Commission's open access policies and comparability principles reflected in the tariff prescribed by this Final Rule. In addition, rates must be consistent with our Transmission Pricing **[31,785]** Policy Statement, and the guidance herein concerning ancillary services.[552]

A final jurisdictional issue raised in the Open Access NOPR concerns buy-sell transactions. We remain concerned, just as we were with buy-sell arrangements in the gas industry, that buy-sell arrangements can be used by parties to obfuscate the true transactions taking place and thereby allow parties to circumvent Commission regulation of transmission in interstate commerce. Thus, we reaffirm our conclusion that we have jurisdiction over the interstate transmission component of transactions in which an end user arranges for the purchase of generation from a third-party. However, we recognize that there is a wide range of programs and transactions that might or might not fall within this category. We will address these on a case-by-case basis.

In summary, the Commission reaffirms and clarifies its prior jurisdictional conclusions and tests for determining the demarcation between federal and state jurisdiction over transmission in interstate commerce and local distribution. We have attempted to address these issues in a way that provides

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[552]In applying the principles of the Final Rule to retail transmission tariffs, the Commission clearly cannot order retail wheeling directly to an ultimate consumer. See FPA section 212(h).

for flexibility and recognition of legitimate state concerns. With regard to retail services, we recognize the states' concerns that the unbundling of retail transactions would result in changes from what historically has been regulated by the states (principally, the rates of transmission assets previously included in retail rate base). However, the decision to provide unbundled retail wheeling is not the Commission's to make because we have no authority to order transmission directly to an ultimate consumer. In addition, even if a retail access program occurs, we do not believe the unbundling of retail transactions will radically change fundamental state authorities, including authority to regulate the vast majority of generation asset costs, the siting and maintenance of generation facilities and transmission lines, and decisions regarding retail service territories. Further, the Commission intends to be respectful of state objectives so long as they do not balkanize interstate transmission of power or conflict with our interstate open access policies. As the electric industry and state regulatory authorities continue to develop new competitive market structures and consider retail wheeling programs, we believe that the tests and mechanisms we have provided in this Rule will accommodate both Federal and state interests and will help provide jurisdictional certainty to market participants.

* * * * *

[31,898]

1. Public Utilities

As with the Open Access Final Rule, there are not a substantial number of public utilities that qualify under the SBA's definition of small electric utility that are subject to the Stranded Cost Final Rule. The Stranded Cost Rule applies only to public utilities that seek stranded cost recovery in connection with a limited set of wholesale requirements contracts (those executed on or before July 11, 1994 that do not contain an exit fee or other explicit stranded cost provision). To the extent that public utilities seek stranded cost recovery, they will do so in a rate filing, where stranded cost recovery is likely to be one of many items considered. Accordingly, the Stranded Cost Final Rule will not pose a significant economic impact on a substantial number of public utility small entities.

2. Non-Public Utilities

With regard to non-public utilities, the stranded cost issue would only arise in a proceeding under sections 211 and 212 of the FPA when, in directing transmission, the Commission addresses the stranded cost issue in determining a just and reasonable rate. As with public utilities, stranded costs will be just one more item to be considered in establishing just and reasonable rates for transmission. As a result, the Stranded Cost Final Rule will not impose a significant economic impact on a substantial number of non-public utility small entities.

C. *Conclusion*

Accordingly, the Commission certifies that these final rules will not have a significant economic impact on a substantial number of small entities.

VII. Information Collection Statement

The Office of Management and Budget's (OMB) regulations[1082] require that OMB approve certain information and recordkeeping requirements (collections of information) imposed by an agency. Upon approval of a collection of information, OMB shall assign an OMB control number and an expiration date. Respondents subject to the filing requirements of this Rule shall not be penalized for failing to respond to this collection of information unless the collection of information displays a valid OMB control number.

There are now approximately 328 public utilities, including marketers and wholesale generation entities. The Commission estimates that 166 of these utilities own, control or operate facilities used for the transmission of electric energy in interstate commerce and would be subject to the filing requirements of this Rule.

Title: FERC-516, Electric Rate Schedule Filings

Action: Final Rule

OMB Control No: 1902-0096

[1082] 5 CFR 1320.11.

Respondents: Public Utilities that own, control or operate facilities used for the transmission of electric energy in interstate commerce.

Frequency of Responses: On occasion.

Necessity of information: The Final Rule requires public utilities that own, control or operate facilities used for the transmission of electric energy in interstate commerce to have on file with the Commission non-discriminatory open access transmission tariffs that contain minimum terms and conditions of service and permits public utilities to make filings to seek recovery of legitimate, prudent and verifiable stranded costs associated with providing open access and FPA section 211 transmission services. The Commission has a mandate under sections 205 and 206 of the FPA to ensure, with respect to any transmission in interstate commerce or any sale of electric energy for resale in interstate commerce by a public utility, that no entity is subject to undue discrimination. The Commission will use the data collected in this collection of information to carry out its responsibilities under Part II of the FPA. The Commission's Office of Electric Power Regulation will use the data to review electric rate and tariff filings.

The Commission is submitting notification of this Final Rule to OMB. Interested persons may obtain information on the reporting requirements by contacting the Federal Energy Regulatory Commission, 888 First Street, N.E., Washington, D.C. **[31,899]** 20426 [Attention: Michael Miller, Information Services Division, (202) 208-1415], and to the Office of Management and Budget [Attention: Desk

Officer for the Federal Energy Regulatory Commission, (202) 395-3087].

VIII. Effective Date

This Rule will take effect on [insert date 60 days after date of publication in the Federal Register]. The Commission has determined, with the concurrence of the Administrator of the Office of Information and Regulatory Affairs of the Office of Management and Budget, that this Rule is a "major rule" within the meaning of section 351 of the Small Business Regulatory Enforcement Act of 1996.[1083] The Rule will be submitted to both Houses of Congress and the Comptroller General prior to its publication in the Federal Register.

List of Subjects

18 CFR Part 35

Electric power rates, Electric utilities, Reporting and recordkeeping requirements.

18 CFR Part 385

Administrative practice and procedure, Electric power, Penalties, Pipelines, Reporting and recordkeeping requirements.

By the Commission. Commissioner Hoecker concurred in part and dissented in part with a separate statement

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[1083] 5 U.S.C. 804(2).

attached. Commissioner Massey dissented in part with a separate statement attached. Lois D. Cashell, Secretary.

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[pp. 31,919 - 31,926]

[31,919]

Appendix C--Allegations of Public Utilities Exercising Transmission Dominance

I. Examples From Proceedings Before Administrative Law Judges

These are examples of allegations that various public utilities have refused to provide comparable service, either through refusals to wheel, dilatory tactics that so protracted negotiations as to effectively deny wheeling, refusals to provide service priority equal to native load, or refusals to provide service flexibility equivalent to the utility's own use.

A. *American Electric Power Service Corp. (AEP)*

In 1993, AEP filed, on behalf of its public utility associate companies, an open access tariff that offered only firm point-to-point service with very limited flexibility. It did not offer network service, flexible point-to-point service, or non-firm service. Thus, it did not provide customers with the same flexibility that AEP itself has. Nor did it provide a service priority equivalent to that enjoyed by native load. The Commission set AEP's tariff for hearing and, on rehearing, held that in order not to be unduly discriminatory, the tariff had to offer comparable service. American Electric **[31,920]**

Power Service Corp., 64 FERC para. 61,279 (1993), reh'g, 67 FERC para. 61,168 (1994).

At hearing, Raj Rao of Indiana Michigan Power Agency (IMPA) (Ex. IMPA-1, Feb 23, 1994) and Kenneth Hegemann of American Municipal Power-Ohio, Inc. (AMP-Ohio) (Ex. AMPO-1, Feb 23, 1994), both senior management officials, testified concerning AEP's alleged discriminatory practices.[1] AMP-Ohio is an association of municipalities in Ohio, some of whose members depend on AEP for transmission and partial requirements service. IMPA is an association of municipalities in Indiana, and many of IMPA's loads are captive to the AEP transmission system. The witnesses alleged as follows:

1. In anticipation of high peak demands, AEP would contract for large blocks of available short-term power, withhold sale of short-term power, refuse to transmit third party short-term power, and require purchases from AEP at the emergency rate (100 mill/kwh) when an emergency might not exist. Ex. AMPO-1 at 6.

2. In December 1989, AMP-Ohio negotiated a 20 MW purchase of short-term power from Louisville Gas & Electric Company (LG&E). AEP refused to wheel because LG&E had earlier that day told AEP it had no power to sell to AEP. AEP

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[1]After the Rehearing Order expanding the scope of the proceeding, AMP-Ohio and IMPA withdrew this testimony as no longer necessary. This withdrawal does not change the fact that the testimony was sworn to under oath.

then bought the power from LG&E and offered to resell it to AMP-Ohio. Ex. AMPO-1 at 6-7.

3. In January 1990, AMP-Ohio solicited bids for February power purchases from a number of utilities including AEP. AEP was not the winning bid. AMP-Ohio made arrangements to purchase the power from four winning bidders and sought transmission through AEP. When AMP-Ohio gave AEP the schedule for delivery, AEP refused to transmit the power, matched the average price of the winning bids, and made the sale itself. Ex. AMPO-1 at 7.

4. In August 1993, an AMP-Ohio member (Columbus, Ohio) was purchasing 10 MW of hourly non-displacement power from AEP and, after AEP raised its price to 60 mills/kwh, sought another source for the next hour. Consumers Power Company and Detroit Edison Company both offered non-displacement power at 40 mills. AEP refused to transmit, saying it had a 600 MW unit out and could not resell power from another source.[2] Columbus cancelled the transaction and had to buy 10 MW of power from AEP at 100 mills/kwh. Ex. AMPO-1 at 7-8.

5. In July 1993, two AMP-Ohio members (Columbus and St. Mary's) had been buying hourly non-displacement

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[2]AEP generally limited its offer of short-term transmission to buy/sell transactions; that is, AEP would buy the power from the seller and resell it to the purchaser. Supplemental testimony of AEP Witness Baker (Ex. A-73) at 27-29. Often, the terms of the buy/sell transaction required transmission dependent utilities (TDUs) to maintain reserves and meet contractual commitments for at least a year. *Id.*

power from AEP when the price rose to 35 mills. Dayton Power & Light Company (DP&L) offered to sell at 23 mills and AEP agreed to transmit for one hour. But for the next hour, AEP said it had problems with its system, refused to transmit the power, kept the power from DP&L for itself and offered to sell power to AMP-Ohio for Columbus and St. Mary's at 100 mills. Columbus increased its local generation, but St. Mary's purchased 8 MW at 100 mills. For the next hour, AMP-Ohio arranged with DP&L for another 8 MW, hoping AEP would transmit under the 24 hour buy-sell agreement. AEP did transmit this power. Seven hours later in the day, St. Mary's Greenup Hydro project power was available and the 8 MW from DP&L was no longer needed. If St. Mary's had been receiving the hourly power that AEP had refused to transmit, St. Mary's could have switched to Greenup power. But because AMP-Ohio had changed to daily service, St. Mary's had to pay a demand charge for the entire day, even though it used the power only 7 hours and would have paid less under the hourly rate. Ex. AMPO-1 at 8-9.

6. In January 1994, AMP-Ohio sought to transfer power from one member with generation to other members, which required transmission over AEP and Toledo Edison lines. Toledo Edison said yes, AEP said no. AMP-Ohio's northern members purchased emergency power from Toledo Edison. AMP-Ohio then reminded AEP that it had agreed not to deny transmission **[31,921]** and AEP agreed to transmit. Ex. AMPO-1 at 9.

7. IMPA arranged to buy 80 MW of short-term power from LG&E and have it wheeled, using buy-sell arrangements, through Public Service Company of Indiana (PSI) and AEP to serve IMPA's load at Richmond (an IMPA

member). The delivered price was $.292 per kW-day plus a 1 mill adder. At the same time AEP arranged to buy 300 MW from PSI at $.30 per kW day plus out-of-pocket energy costs. Hence, PSI was shipping a total of 380 MW to AEP with 80 MW of that amount to be delivered to IMPA's load at Richmond. Then, on a day when IMPA should have received the 80 MW, AEP told IMPA that PSI had sold everything to AEP and that IMPA would have to buy from AEP at $.63 per kW day plus the cost of energy from AEP. IMPA purchased from AEP under protest. AEP used its control over transmission to intercept the 80 MW at a lower price and resell it as short-term power to IMPA. AEP claimed that PSI had terminated its sales to AEP on that day. But the 80 MW was independent of PSI's other sales to AEP and would not have been interrupted if AEP had not interrupted it. IMPA-1 at 7.

8. IMPA has combustion turbines owned by and located at one member, which IMPA would like to connect to the Joint Transmission System owned by IMPA, CINergy and Wabash Valley Power Association. To do so, IMPA needed a metering agreement with AEP, to which AEP would not agree. IMPA-1 at 6.

9. In January 1994, IMPA had power to sell from its turbines when AEP and others needed power. IMPA offered power to AEP but AEP it said could not purchase the power without an existing contract. Moreover, since there was no short-term tariff, IMPA could not sell the power to another utility. IMPA-1 at 6.

10. Another example of the utility engaging in dilatory tactics that raised the customer's transaction costs and

effectively denied transmission is the "sham transaction" provision proposed by AEP. As filed, AEP's tariffs permitted it to deny service merely because a portion of the transmitted power might be used to serve a former retail customer of AEP. See, e.g., Ex. BR&WVP-1 (J. Bertram Solomon testimony, February 23, 1994). (As part of a settlement AEP filed the pro forma tariff and withdrew this provision.)

11. Finally, AEP's originally filed tariff contained a "prodigal customer" provision. Under this provision, transmission customers who sought to convert back to requirements service had to give AEP five years' notice, in which case AEP and the customer would enter into negotiations to determine whether AEP will provide service at all and if so under what rate, terms, and conditions. Ex. S-39 at 1 (Staff testimony). AEP did not require notice from all new customers, only from prodigal customers. Id. at 2. That a potential customer was previously served by AEP is not a reason to treat the customer differently. (AEP withdrew this provision when it filed the pro forma tariff.)

B. *Entergy Services, Inc. (Entergy)*

Entergy filed a partial settlement largely adopting the NOPR pro forma tariffs except for two provisions (headroom and ancillary services). Because the settlement predated the filing date for customer testimony before the ALJ, the customers did not address the need for Entergy to file a tariff. However, customers did make allegations of discriminatory practices, as follows.

1. Customers alleged that Entergy flat-out refused to wheel. Louisiana Energy and Power Authority (LEPA)

witness Sylvan J. Richard testified that LEPA's predecessor systems could not obtain interconnections from Entergy. Ex. SJR-1 at 50.

2. Customers also alleged that Entergy refused to provide service priority equal to native load and refused to provide service flexibility equivalent to the utility's own use. For example, LEPA witness Richard testified that even after state commissions ordered interconnections and other coordination services, LEPA's predecessors were still not able to obtain coordination services because Entergy was not willing to coordinate and because the transmission service it did offer was inflexible, unidirectional point-to-point service, which prevented economic coordination with others. Id. at 50-51.

3. South Mississippi Electric Power Association (SMEPA) witness J. Bertram Solomon testified that Entergy's original "open access" tariff was restricted to **[31,922]** point-to- point service, proposed separate charges for each operating company, and required the cancellation of existing agreements in order to take service under the proposed tariff. Ex. SMEPA-10 at 28. Entergy eventually filed a network tariff, but proposed different local facilities charges for the various Entergy public utility operating subsidiaries. Id. at 29. Since these local facilities charges were higher than the transmission component of the subsidiaries' bundled rates, Entergy obtained a competitive advantage. Id.

4. The Arkansas Cities and Cooperatives (ACC) is a group of cities and cooperatives that own or operate electric generation or distribution systems in Arkansas. ACC Witness Steven Merchant testified that Entergy has segregated the

wholesale market between two of its subsidiaries, Arkansas Power & Light Copmpany (APL) and Entergy Power, Inc. (EPI). Ex. SMM-1 at 16. In marketing power and energy in Arkansas, EPI is subject to an Arkansas Commission order that bars EPI from competing with APL for wholesale loads without first obtaining a waiver. Id. Recently, EPI requested this waiver for all wholesale transactions in Arkansas except for wholesale customers currently served by an Entergy subsidiary; in other words, EPI requested the Arkansas Commission to expand competition for all wholesale customers except where EPI might compete with APL. Id. ACC witness Merchant concluded that, since EPI does not compete with APL, Entergy insulates APL's wholesale business from competition and denies those wholesale customers access to EPI as a source of power, thereby limiting alternative generation sources available to ACC. Id. at 17-19. (Entergy's witness Kenney stated that Entergy has recently filed a joint motion with ACC to the Arkansas Commission seeking to extend the waiver and permit EPI to sell to APL's wholesale customers. Ex. JFK-11 at 14- 15.)

C. *Pacific Gas & Electric Company (PG&E)*

Northern California Power Agency (NCPA) attached several documents to its 1988 complaint in Docket No. EL89-4. These documents were provided to support NCPA's claim that PG&E's unreasonable practices under the PG&E/NCPA Interconnection Agreement (IA) effectively denied NCPA access to transmission properly requested under the IA. Although the parties eventually settled and the Commission terminated the docket with a letter order dated May 18, 1988, these documents provide allegations of PG&E using dilatory

tactics that so protracted negotiations as to effectively equal a refusal to wheel.[3]

1. PG&E stated that since transmission was not currently available, it was entitled to wait 72 months before providing transmission; that is, transmission access could not be granted before the passing of the 72-month notice period. NCPA 1988 Complaint, Ex. 3. However, the IA provided that transmission be provided when it becomes actually available. PG&E also requested substantial additional information, which NCPA considered beyond that reasonably necessary for a study, but still provided. PG&E then determined that transmission was not available, reasoning that transmission was unavailable unless all the transmission requested could be provided 8760 hours per year without restrictions or limitations, extending through the expiration of the agreement in 2013. NCPA 1988 Complaint at 9.

2. On November 27, 1987, NCPA made a new transmission request to PG&E, seeking 50 MW of bi-directional transmission at Midway. NCPA 1988 Complaint, Ex. 5. On January 28, 1988, PG&E filed an interconnection agreement with Turlock Irrigation District (TID) that provided TID with 50 MW of bi-directional transmission at

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[3]All of these incidents are related to and examples of PG&E's conduct described in the NOPR (*FERC Statutes and Regulations* ¶32,514 at p. 33,073 n.151), that is, the history of PG&E's attempt to avoid its commitments made to the California owners of the California Oregon Transmission Project (COTP). However, these incidents are not exactly the same as the incidents described in the NOPR, because NCPA is not one of the owners of the COTP.

Midway. Pacific Gas & Electric Company, 42 FERC para. 61,406, order on reh'g, 43 FERC para. 61,403 (1988). On February 22, 1988, PG&E advised NCPA that all firm transmission service available at Midway had **[31,923]** been fully subscribed. NCPA 1988 Complaint, Ex. 6. Then, on March 29, 1988, PG&E filed with the Commission an interconnection agreement with Modesto Irrigation District (MID), that provided MID with 50 MW of bi-directional transmission at Midway. Pacific Gas & Electric Company, 44 FERC para. 61,010 (1988). At about the same time (in the last week in March 1988), PG&E advised NCPA that the allocations of transmission to TID, MID, and others, including a not yet finalized allocation to Sacramento Municipality Utility District, had used all the transmission available at Midway. NCPA 1988 Complaint, Exs. 7 and 8.

D. *Northeast Utilities Service Company (NU)*

This is the case where Northeast Utilities acquired Public Service of New Hampshire (PSNH) (Docket No. EC90-10). New England Power Company (NEP) witness Robert Bigelow's direct testimony expressed concern over the "relatively restrictive transmission policies of both" NU, on behalf of Northeast Utilities' public utility subsidiaries, and PSNH. Bigelow Direct Testimony at 21 (filed May 25, 1990). In his cross rebuttal testimony, Mr. Bigelow testified that "NU has a poor track record as a provider of transmission service" and "PSNH also has an abhorrent track record as a provider of transmission services." Bigelow Cross Rebuttal Testimony, at 3 (filed June 20, 1990). Mr. Bigelow described both NU's and NEP's (his own company) failure to provide service flexibility equivalent to their own use. Except for NEP's TDUs, both NEP and NU historically provided only

point-to-point transmission, which required separate scheduling for each transaction. Bigelow Cross Rebuttal at 4.

E. *Southern California Edison Company and San Diego Gas and Electric Company*

The evidence in this merger proceeding (Docket No. EC89-5) included testimony from a number of witnesses describing instances of Edison's conduct. Richard Greenwalt was the power supply supervisor for the City of Riverside, California. He was responsible for scheduling all purchases of energy for Riverside and for the cities of Azusa, Banning and Colton, California. Greenwalt testimony at 1 (November 1989). (These four cities and Anaheim, California, are collectively referred to as the Southern Cities or Cities.) Joseph Hsu was the Director of Utilities for Azusa. Hsu testimony at 1 (November 1989). Gale Drews was the electric utility director of Colton. Drews testimony at 1-2 (November 1989). Bill Carnahan was the director for Riverside. Carnahan testimony at 1 (November 1989). Gordon Hoyt was the general manager of the Anaheim power department. Hoyt testimony at 1 (November 1989). Dan McCann was the power coordination supervisor for Anaheim. He supervised Anaheim's load scheduling and is a former Edison employee, having worked for Edison for 20 years. McCann Testimony at 1-2 (November 1989). These witnesses testified that Edison refused to wheel as follows.

1. Edison's policy was to curtail the Cities any time it could be justified using any of a list of acceptable reasons to deny interruptible transmission service. Id. at 22-23.

2. Edison would not generally provide transmission service when Edison could save money by itself purchasing the economy energy that would be wheeled. McCann testimony at 19. The Cities called Edison every hour to request interruptible transmission service. Id.. Edison often refused to sell energy available in the Western Systems Power Pool to the Cities and then made available higher cost contract energy or partial requirements service. Id. at 19-20.

3. When Anaheim requested Edison provide firm transmission of power from neighboring states, Edison would often agree to provide non-firm service but would not integrate the capacity for many years in the future, saying that its control area did not need capacity at that time. Hoyt testimony at 9. Since the selling utility was interested in a sale of capacity, not just energy, the transaction would not occur. Id. Edison repeatedly used its control over transmission to deny Anaheim access to low-cost firm power. Id. at 9-10.

4. While Edison provided short-term firm transmission service to the Cities, it would only provide long-term firm service for three specific resources: The SONGS nuclear plant, a specific IPP, and Hoover Dam power. Hoyt testimony at 20. One of Edison's reasons for denying long-term transmission was that Edison desired to **[31,924]** reserve the transmission for its own future (unspecified) needs. Id.

5. In the 1970s, Edison refused to allow the Cities access to the Pacific Intertie. Hoyt testimony at 21; Drews testimony at 7-8.

6. In 1988, Edison refused to provide transmission service for a Cities power purchase from Public Service

Company of New Mexico (PSNM) from Palo Verde Nuclear station. Hoyt testimony at 21.

7. Edison has refused to provide requested firm transmission from

--California-Oregon border to Midway Station

--Nevada-Oregon Border to Sylmar Substation

--Palo Verde Switchyard to Vista

--SONGS Switchyard to Vista.

Carnahan testimony at 15.

8. Riverside requested transmission from Palo Verde and was told that such service was not available. Carnahan testimony at 16. Edison offered Riverside only 12 MW of curtailable transmission entitlement to provide Riverside's share of Palo Verde. Id. This service was neither large enough or long enough, and Edison insisted on unreasonable terms and conditions. Id.

9. Azusa, Banning and Colton had a contract with Edison that entitled them to use their Palo Verde firm transmission path to schedule energy to meet their contract energy obligation. Edison refused to permit the three cities to use that path. Edison did not contest that the contracts allowed this use, but said that the scheduling of such small amounts of energy for the three cities would be too burdensome. Greenwalt testimony at 14.

10. Edison would not respond in a timely manner to the Cities' requests, routinely taking months to respond. Drews testimony at 15.

11. During the 1980s, Edison provided Colton with some transmission service to allow the Cities to reach certain suppliers, but limited the choices available to the Cities and imposed terms and conditions that increased the Cities' costs and placed Colton at a disadvantage against Edison. Drews testimony at 9. Arranging alternative generation sources was difficult because the Cities always had to first get Edison to state whether it would provide transmission.

12. During 1988 and 1989, a dispute arose between Edison and the Cities concerning the Hoover Uprating Project. Drews testimony at 16. Edison argued that for the months when units were out of service for uprating, and Southern Cities capacity was reduced to zero, Southern Cities would not receive an energy credit, even though energy was still available and used by Edison. But the contracts allowed a participant who did not have capacity to still schedule its energy as non-firm energy on the capacity of another participant. Id. at 16-17.

13. In 1986, Azusa negotiated a power purchase contract with the California Department of Water Resources in increments of first 5 MW and then 2 MW (for a total of 7 MW). Hsu testimony at 14. First Edison assured Azusa that the transmission for the additional 2 MW would not be a problem. Id. Then Edison would not agree to amend the transmission service agreement for the additional 2 MW. Id.

14. In 1986, Azusa notified Edison of Special Condition 12[4] purchases from PG&E and requested firm transmission service. Id. Two months before service was to begin, Edison notified the Cities of a problem with the transmission lines. Id. Transmission was eventually granted, but only after a four-month delay and substantial losses to the Cities. Id. Then Edison decided there was no problem with its transmission facilities. Id. at 14-15.

15. In 1986-87, the Cities purchased 20 MW from PG&E and 80 MW from Deseret G&T Cooperative. Hoyt testimony at 7-8. Edison stated that without reinforcement of its transmission system, Edison would not provide the transmission. Id. There was a five-month delay during which the Cities were forced to purchase from Edison at a higher cost. Id. at 8-9. Then Edison decided that the transmission system did not need reinforcement. Id. at 8.

[31,925]

16. Edison also refused to provide a service priority equal to that of native load. It would curtail the Cities in order to purchase more economy energy for itself. McCann testimony at 28. If Edison could make the purchase, it would curtail the City and use the energy for itself. Id. When Edison curtailed the Cities, they were not able to purchase economy energy and instead purchased energy from Edison. Id. at 24.

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[4]Special Condition 12 of the Integrated Operations Agreement between Edison and the Southern Cities defined certain Special Condition 12 resources and allowed the Cities to make certain uses of those resources, subject to certain restrictions.

17. According to Edison, the interruptible transmission it provided the Cities was interruptible for any reason. Id. at 20. A purchase could be terminated the hour after it is begun or even during the hour. Id. As a result, the Cities lost opportunities to make advantageous economy purchases. Id. at 20-21.

18. Edison also refused to provide customers flexibility similar to the flexibility Edison provided itself. Edison's refusal to provide bi-directional transmission service restricted the Cities' abilities to purchase hydroelectric energy from the Pacific Northwest. Hoyt testimony at 22. Because most contracts with Northwest utilities require a return of power, the Northwest utilities would not deal with the Cities without transmission to return energy. Id. at 22-23. Edison did provide bi- directional transmission to the Los Angeles Department of Water & Power (LADWP) to accommodate flows to and from Arizona. Id.

19. Riverside was unable to obtain non-firm service more than two hours in advance of need. Carnahan testimony at 18.

20. Riverside and Colton were both served out of Edison's Vista substation. Although the two cities were on the same 69 kV bus, Edison would not allow them to sell energy to each other. Greenwalt testimony at 17.

21. Riverside's agreement with Edison allowed Riverside to purchase a block of energy through the WSPP and divide it up among the four Cities (Azusa, Banning, Colton and Riverside). Greenwalt testimony at 17. When Riverside had excess energy from other sources, Edison

would not permit it to sell that energy to the other three cities. Id. For example, Riverside attempted to sell Deseret energy transmitted by LADWP to the Edison system. Id. at 17-18. LADWP would not break out the Cities' shares of that energy, and Edison would not accept the energy as a delivery for all four cities. Id. at 18. Edison argued that because this energy was excess energy that Riverside could not use, Riverside did not have transmission rights to bring it into the control area. Id. As a result, Riverside paid for the energy delivered by LADWP to the Edison control area, but could not sell it to the other three cities, and gave it to Edison itself, which consumed the energy without making any payment for it. Id. Riverside tried a number of alternative paths, including using WSPP transmission where Riverside paid Edison 5 mills to connect to Azusa, 5 mills to connect to Banning, and 5 mills to connect to Colton for each megawatthour. While this approach was successful for a while, eventually Edison refused to permit these sales.

22. Edison claimed that the Cities only have transmission rights to bring in enough Special Condition 12 energy to satisfy the Cities' load. Greenwalt testimony at 18.

23. Edison contended that the Cities' load requirements were satisfied first by integrated resources and then by Special Condition 12 and economy energy purchases. Id. at 19. When the Cities' integrated resources exceeded their load, any Special Condition 12 resources became excess. Under Riverside's Deseret contract, the Cities were required to take a minimum of 35 MW each hour. Id. Edison acknowledged that it was obligated to buy, or allow the Cities to sell, any excess energy from Riverside's integrated resources. Id. However, Edison refused to give the Cities

credit for excess Special Condition 12 energy brought into the area, claiming that the Cities could not have brought it in because they did not have transmission rights. Id.

II. Other Examples of Transmission Disputes

Disputes over transmission are not uncommon, contrary to EEI's suggestion. Some recent examples taken from pleadings and other documents and from Commission orders reveal that it has been very difficult for various entities in the electric power industry to agree on transmission rights. These examples also reveal that even after issuance of AEP and the Open Access NOPR with its proposed pro forma tariffs, there has been considerable controversy over whether various utilities' **[31,926]** "open access" tariffs deviate from those tariffs. (The Commission has allowed utilities that adopt tariffs that match or exceed the non-rate terms and conditions in the NOPR pro forma tariffs to obtain certain benefits.)

A. In a letter of February 3, 1995 to Mr. Gerald Richman of the Commission's Enforcement section in the Office of the General Counsel, Steven J. Kean, Vice President, Regulatory Affairs, Enron Power Marketing, Inc. (Enron) alleged that Niagara Mohawk Power Corporation (NiMo) refused to wheel power from Rochester Gas & Electric (RG&E) to Enron under RG&E's transmission contract with NiMo; however, when Enron revealed the buyer, NiMo did wheel power for RG&E to the buyer. Mr. Kean alleged that this was not an isolated incident. NiMo argued that the contract did not require it to provide RG&E with transmission to Enron. It also said that the principle of comparability does not require the service. Letter of

November 21, 1994 from NiMo representative A. Karen Hill to Gerald Richman.

B. The Commission's Task Force Hot Line (Hot Line) received a complaint that a member of the New York Power Pool (NYPP) refused to transmit power that another member bought from a power marketer. In a letter of November 17, 1994, from Chair Moler to Mr. William J. Balet, Executive Director of NYPP, Chair Moler explained that the Commission's enforcement staff had investigated and found the allegation to be true.

C. In Southern Minnesota Municipal Power Agency v. Northern States Power Company (Minnesota), 73 FERC 61,350 (1995), NSP and SMMPA had a contract under which NSP agreed to provide transmission service. However, the parties had numerous disputes over the service. The Commission found that NSP had misinterpreted the contract in several ways. For, example, SMMPA argued that it should be able to directly schedule its deliveries of energy out of the NSP control area and that it should not be limited to particular points of delivery. NSP argued that only it was entitled to control the physical operation of scheduling. The Commission found that the clear language of the contracts gave SMMPA the authority to schedule its own power.

D. Mid-Continent Area Power Pool, 72 FERC para. 61,223 (1995), involved MAPP's membership criteria, which made it impossible for a power marketer to join MAPP and obtain the benefits of certain transmission services available only to MAPP members. The Commission found that the membership criteria may be unreasonable, particularly since

there may be less burdensome ways of setting up membership criteria for non-traditional entities.

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[pp. 31,966 - 31,981]

[31,966]

APPENDIX G

I. Legal Analysis of Commission Jurisdiction Over the Rates, Terms and Conditions of Unbundled Retail Transmission in Interstate Commerce

Based on an analysis of the relevant legislative history and case law under the Federal Power Act (FPA), the Commission concludes that it has exclusive jurisdiction over the rates, terms and conditions of the unbundled transmission in interstate commerce, by a public utility, of electric energy to an end user. This is also known as retail wheeling in interstate commerce.[1]

The Commission's jurisdiction over the rates, terms and conditions of transmission in interstate commerce derives

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[1]Section 212(h) of the FPA provides that no order issued under the FPA shall be conditioned upon or require the transmission of electric energy directly to an ultimate consumer. 16 U.S.C. §824k(h). The Commission's assertion of jurisdiction in this final rule is over the rates, terms and conditions of retail transmission that occurs voluntarily or as a result of a state retail access program.

from Congress' power to regulate interstate commerce under the United States Constitution[2] and the FPA. When Congress enacted the FPA, it gave the Commission exclusive jurisdiction over the rates, terms and conditions of transmission in interstate commerce by public utilities. The Supremacy Clause of the Constitution provides that federal laws enacted pursuant to the powers delegated to the federal government by the United States Constitution are the supreme law of the land.[3] Accordingly, to the extent that retail wheeling involves transmission in interstate commerce by public utilities, the rates, terms and conditions of such service are subject to the exclusive jurisdiction of the Commission, and must be filed with the Commission.[4]

1. Relevant Federal Power Act Provisions

Section 201(b)(1) of the FPA provides:

The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * *. The Commission shall have jurisdiction over all facilities for such transmission or sale of electric energy, but shall not have jurisdiction * * * over facilities used in local distribution or only for the transmission of electric energy in

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[2]U.S. Const. art I, Section 8, cl.3.

[3]U.S. Const. art. VI, cl.2.

[4]*See Montana-Dakota Utilities Co. v. Northwestern Public Service Co.*, 341 U.S. 246, 251-52 (1951) (*Montana-Dakota*).

interstate commerce, or over facilities for the transmission of electric energy consumed wholly by the transmitter.

16 U.S.C. 824(b)(1) (emphasis added). Thus, the statute on its face limits Commission jurisdiction over sales of energy to sales at wholesale, but does not limit jurisdiction **[31,967]** over transmission to transmission used only for wholesale sales.

Sections 201(c) and (d) define the meaning of "the transmission of electric energy in interstate commerce" and "sale of electric energy at wholesale in interstate commerce." Section 201(c) provides:

For the purpose of this Part, electric energy shall be held to be transmitted in interstate commerce if transmitted from a State and consumed at any point outside thereof: but only insofar as such transmission takes place within the United States.

16 U.S.C. 824(c). Section 201(d) provides:

The term "sale of electric energy at wholesale" when used in this Part means a sale of electric energy to any person for resale.

16 U.S.C. 824(d).

Sections 205 and 206 of the FPA give the Commission jurisdiction over the rates, terms and conditions of transmission in interstate commerce, and sales at wholesale in interstate commerce, by public utilities. 16 U.S.C. 824d and 824e.

2. Legislative History and Case Law

Much of the legislative history of the FPA indicates that Congress intended the Commission's jurisdiction to extend only to those matters which the Attleboro decision[5] held to be beyond the reach of the States. For instance, the report accompanying the Senate bill states that subsection (b) "leaves to the States the authority to fix local rates even in cases where the energy is brought in from another State."[6] In other words, states retain authority to regulate rates of electric energy to ultimate consumers. The Senate report also states:

The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy[7] for interstate transmission and sale.

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[5]*Public Utilities Commission v. Attleboro Steam & Electric Co.*, 273 U.S. 83 (1927) (Attleboro). In Attleboro, the Supreme Court held that State regulation of the interstate sale of electricity was barred by the Commerce Clause because such regulation would impose a "direct burden" on interstate commerce.

[6]S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935). See also H.R. Rep. No. 1318, 74th Cong., 1st Sess. 8 (1935).

[7]The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

S. Rep. No. 621, 74th Cong., 1st Sess. 48 (1935) (emphasis added). Thus, federal jurisdiction over transmission lines is not dependent on whether those lines are used to effect a sale, wholesale or otherwise.

The provisions of FPA section 201 reserving certain regulatory authority to the States have been interpreted narrowly.[8] The Supreme Court has stated:

In section 201(b), Congress did no more than leave standing whatever valid state laws then existed relating to the exportation of hydroelectric energy; by its plain terms, 201(b) simply saves from pre-emption under Part II of the Federal Power Act such state authority as was otherwise "lawful."[9]

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[8]Section 201(a) declares that Federal regulation of the transmission of electric energy in interstate commerce and the sale of such energy at wholesale in interstate commerce is necessary in the public interest, "such Federal regulation, however, to extend only to those matters which are not subject to regulation by the States." 16 U.S.C. §824(a). Section 201(b)(1) states that the provisions of Part II of the FPA apply to the transmission of electric energy in interstate commerce and the sale of electric energy at wholesale in interstate commerce but, except as specifically provided, "shall not apply to any other sale of electric energy or deprive a State or State commission of its lawful authority now exercised over the exportation of hydroelectric energy which is transmitted across a State line." 16 U.S.C. §824(b)(1).

[9]*New England Power Co. v. New Hampshire*, 455 U.S. 331, 341 (1982) (NEPCO).

The Court also stated:

Nothing in the legislative history or language of the statute evinces a congressional intent 'to alter the limits of state power otherwise imposed by the Commerce Clause,' * * * or to modify the earlier holding of this Court concerning the limits of state authority to restrain interstate trade.[10]

[31,968]

Unlike the narrow interpretations given to the FPA provisions reserving certain regulatory authority to the States,[11] the courts have construed transmission "in interstate commerce" broadly. The term does not turn on whether the contract path for a particular power or transmission sale crosses state lines, but rather follows the physical flow of electricity. Because of the highly integrated nature of the electric system, this results in most transmission of electric energy being "in interstate commerce."

One of the earliest cases construing Commission jurisdiction over transmission was Jersey Central Power & Light Co. v. FPC, 319 U.S. 61 (1943) (Jersey Central). In that case, the Commission asserted jurisdiction over a New

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[10] *Id.* (citation omitted).

[11] While Congress may exercise its Commerce Clause authority to grant the States that "ability to restrict the flow of interstate commerce that they would not otherwise enjoy," Lewis v. BT Investment Managers, Inc., 447 U.S. 27, 44 (1980), States may not exercise such regulatory powers unless Congress has expressly stated its intention to make such an affirmative grant of power. *NEPCO*, 455 U.S. at p. 343.

Jersey utility by showing that the utility owned transmission facilities that were used to transmit energy in interstate commerce. The Court found that the Commission had demonstrated that the utility owned transmission facilities that were indirectly interconnected, through a second New Jersey utility, to facilities owned by a New York utility and that the facilities were used to transmit electric energy in interstate commerce.

The Court noted that section 201(c) of the FPA defines electric energy transmitted in interstate commerce to be energy "transmitted from a State and consumed at any point outside thereof." The Court stated:

It is impossible for us to conclude that this definition [of transmission in interstate commerce] means less than it says and applies only to the energy at the instant it crosses the state line and so only to the facilities which cross the line and only to the company which owns the facilities that cross the line.

319 U.S. at 71. Thus, a critical question regarding the jurisdictional status of a wheeling transaction is whether the facilities used to provide the service transmit electric energy in interstate commerce.

In Connecticut Light & Power Co. v. FPC, 324 U.S. 515 (1945) (CL&P), the Court reviewed the Commission's finding that a Connecticut utility was jurisdictional because it owned transmission facilities that were used in interstate commerce. The Court generally embraced the Jersey Central standard for determining whether facilities are used to transmit electric energy in interstate commerce. The Court

emphasized that whether certain facilities transmit electric energy in interstate commerce is more a technical than a legal question. The Court stated:

> Federal jurisdiction was to follow the flow of electric energy, an engineering and scientific, rather than a legalistic or governmental, test.

324 U.S. at 529. Thus, the Court adopted the Jersey Central test providing that the Commission's jurisdiction generally extends to transmission facilities that transmit electric energy in interstate commerce.

The Court also applied the Jersey Central test in FPC v. Florida Power & Light Co., 404 U.S. 453 (1972), affirming the Commission's finding of jurisdiction over a Florida utility. The Commission demonstrated that the utility transmitted power to another Florida utility's "bus"[12] that power was simultaneously transferred from the "bus" to a Georgia utility. The Court upheld the Commission's finding that electric energy from the two Florida utilities was commingled and was therefore transmitted in interstate commerce. 404 U.S. at 463.

In all of the above cases, the Court's decisions turned on whether energy being transmitted flowed in interstate commerce as a technical matter. The decisions did not turn on

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[12]A bus is an electrical conductor which serves as a common connection for two or more electrical circuits. Electric Utility Rate Design Study, Glossary: Electric Utility and Ratemaking Load & Management Terms, Edison Electric Institute (Sept. 11, 1978).

whether the transmission of energy flowing in interstate commerce involved energy that was being sold for resale or was being sold to **[31,969]** an end user. Thus, there is nothing in the statute, its legislative history, or the case law to indicate that the Commission's jurisdiction over rates, terms and conditions of transmission in interstate commerce extends only to wholesale transmission and not retail transmission. Indeed, the statute on its face gives the Commission jurisdiction over transmission in interstate commerce and makes no distinction between wholesale transmission and retail transmission.

However, there are two important limitations on Commission authority. First, as discussed above, the FPA does not give the Commission jurisdiction over sales of electric energy at retail. Such sales historically have been bundled sales (i.e., generation and transmission), and courts and the Commission have recognized State jurisdiction over bundled sales of energy. Second, under section 201(b)(1) of the FPA, the Commission does not have jurisdiction over facilities used in local distribution. In CL&P, the Court stated that local distribution facilities are exempt from Commission jurisdiction even if those facilities "carry no energy except extra-state energy." 324 U.S. at 531.

In the next section the Commission further discusses the statutory provisions and case law that shed light on the demarcation between transmission and local distribution, and thus on the jurisdictional line between federal and State authority.

II. Legal Analysis of Commission Jurisdictional Transmission Facilities and State Jurisdictional Local Distribution Facilities

Two specific circumstances are addressed:

First, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

Second, what facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to an end user?

Based on an analysis of the relevant legislative history and case law under the FPA, the Commission reaches the following conclusions. With respect to the first circumstance, the Commission concludes that a public utility's facilities used to deliver electric energy to a wholesale purchaser, whether labeled "transmission," "distribution," or "local distribution" are subject to the Commission's exclusive jurisdiction under sections 205 and 206 of the FPA, and that a public utility's facilities used to deliver electric energy from the wholesale purchaser to the ultimate consumer are "local distribution" facilities subject to the rate jurisdiction of the state.[13]

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[13]There are, of course, facilities that are used to provide delivery to both wholesale purchasers and end users. In those situations, we believe that the Commission and the States have

With respect to the second circumstance, the Commission believes that, based on the particular facts of the case, some of the public utility's facilities used to deliver electric energy to an end-user may be FERC-jurisdictional transmission facilities, while some of the facilities used may be state-jurisdictional local distribution facilities.

We set forth below the relevant legislative history and case law, our legal conclusions, and the factors which we believe are indicative of whether facilities are used in "local distribution" or "transmission in interstate commerce," as those terms are used in the FPA.

1. Relevant Federal Power Act Provisions

The Commission's jurisdiction is set forth in section 201 of the FPA.[14] Section 201(b)(1) provides in pertinent part:

The provisions of this Part shall apply to the transmission of electric energy in interstate commerce and to the sale of electric energy at wholesale in interstate commerce * * *. The Commission shall have jurisdiction over all facilities for **[31,970]** such transmission or sale of electric energy, but shall not have jurisdiction * * * over facilities used in local distribution or only for the transmission of electric energy in intrastate commerce, or over facilities for

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jurisdiction to set rates for the services that are within their respective jurisdictions. That facilities are used to serve resale and retail customers does not, however, necessarily mean that the facilities are local distribution facilities.

[14]16 U.S.C. §824.

the transmission of electric energy consumed wholly by the transmitter.[15]

Some of the court decisions that construe jurisdictional facilities under section 201 also construe the Commission's jurisdiction under section 203. Section 203(a) provides, in relevant part:

No public utility shall sell, lease, or otherwise dispose of the whole of its facilities subject to the jurisdiction of the Commission, * * * or by any means whatsoever, directly or indirectly, merge or consolidate such facilities or any part thereof with those of any other person * * * without first having secured an order of the Commission to do so.[16]

In addition, section 206(d) concerns facilities "under the jurisdiction of the Commission":

The Commission upon its own motion, or upon the request of any State commission whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy.[17]

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[15]16 U.S.C. §824(b) (emphasis added).

[16]16 U.S.C. §824b (emphasis added).

[17]16 U.S.C. §824e(d) (emphasis added).

2. Legislative History of the FPA

The relevant legislative history of the general purposes of Title II of the FPA, and of section 201 in particular, focuses primarily on bundled sales of electric energy and does not directly address the issue of what constitutes local distribution as opposed to transmission in interstate commerce.

In discussing the general purposes of Title II of the House bill, the House Report states:

Title II * * * establishes for the first time regulation of electric utility companies transmitting energy in interstate commerce.

* * * * *

* * * Under the decision of the Supreme Court of the United States in (Attleboro), the rates charged in interstate wholesale transactions may not be regulated by the States. Part II gives the Federal Power Commission jurisdiction to regulate these rates. A "wholesale" transaction is defined to mean the sale of electric energy for resale and the Commission is given no jurisdiction over local rates even where the electric energy moves in interstate commerce.[18]

[18]H.R. Rep. No. 1318, 74th Cong., 1st Sess. 7-8 (1935).

In its analysis of section 201, the House Report states:

As in the Senate bill no jurisdiction is given over local distribution of electric energy, and the authority of States to fix local rates is not disturbed even in those cases where the energy is brought in from another State.[19]

The Senate Report's discussion of the general purposes of the FPA states:

The decision of the Supreme Court in [Attleboro] placed the interstate wholesale transactions of the electric utilities entirely beyond the reach of the States. Other features of this interstate utility business are equally immune from State control either legally or practically.[20]

In discussing material differences between the final version of the Senate bill and the original version, the Senate Report states:

Subsection (b), formerly (a), which states the subject matter to which the part relates, has been clarified to make plain that it includes interstate transmission where there is no sale and excludes **[31,971]** all facilities used only for

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[19]*Id.* at p. 27.

[20]S. Rep. No. 621, 74th Cong., 1st Sess. at p. 17 (1935). See id. at p. 18 ("The revision [between the original and final versions of the Senate bill] has also removed every encroachment upon the authority of the States. The revised bill would impose Federal regulation only over those matters which cannot effectively be controlled by the States.")

production of transmission in intrastate commerce or in local distribution.[21]

In discussing section 201 of the Senate bill, the Senate Report further states:

The rate-making powers of the Commission are confined to those wholesale transactions which the Supreme Court held in (Attleboro) to be beyond the reach of the States. Jurisdiction is asserted also over all interstate transmission lines whether or not there is sale of the energy carried by those lines and over the generating facilities which produce energy for interstate transmission and sale. It is obvious that no steps can be taken to secure the planned coordination of this industry on a regional scale unless all of the facilities, other than those used solely for retail distribution, are made subject to the jurisdiction of the Commission. Facilities used only for intrastate commerce or local distribution are expressly excluded from the operation of the act.[22]

The Conference Report adds little description regarding jurisdictional facilities. In reference to section 201(b) it states that:

[T]he language of the House amendment has been followed with a clarifying phrase added to remove any doubt as to the Commission's jurisdiction over facilities used for the

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[21] *Id.* at p. 19.

[22] *Id.* at p. 48. The provisions of the Senate bill regarding federal jurisdiction over generating facilities were eliminated from the final version of the bill.

generation and local distribution of electric energy to the extent provided in other sections of this part and the part next following.[23]

In addition to the above statements pertaining to section 201 of the FPA, Congress referenced distribution of energy in the legislative history of section 206(d). Section 206(d) was originally enacted as section 206(b) of the FPA. Under the Regulatory Fairness Act of 1988,[24] section 206(b) was redesignated as section 206(d).

The Conference Report on the original FPA does not address section 206(b). The Senate Report on the FPA bill states in pertinent part:

Subsection (b) authorizes the Commission to investigate and determine the cost of the production or transmission of electric energy by means of facilities under the jurisdiction of the Commission in cases where the Commission has no authority to establish a rate governing the sale of such energy. * * * Since the rate-making powers granted to the Commission apply only to the wholesale rates of energy sold in interstate commerce, this last subsection should be of great benefit in removing the practical difficulty which the States may encounter in regulating the interstate distribution rates which are left under their control. Such rate regulation involves the examination and valuation of property outside the State. The task is one requiring an agency with a

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[23]H.R. Conf. Rep. No. 1903, 74th Cong., 1st Sess. 74 (1935).

[24]Pub. L. No. 100-473, 102 Stat. 2299 (1988).

jurisdiction broader than that of a single State. The authority of the Federal Commission is to render assistance to the State commissions in a way which would preserve and make more effective the jurisdiction which is thus left to the States.[25]

The House Report discusses section 206(b) as follows:

This subsection reaches those situations where electric energy is transmitted in interstate commerce by the same company which distributes it locally, and will greatly aid State commissions in fixing reasonable rates in such cases.[26]

Thus, the discussions in the two reports do not appear to contemplate a situation in which the transmitter and seller of electric energy are different, and neither is a "local" distributor. The House Report expressly refers to the same company being the transmitter and seller of electric energy. The Senate Report by its terms addresses the regulation of interstate distribution rates.[27]

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[25]S. Rep. No. 621, 74th Cong., 1st Sess. 51 (1935) (emphasis added).

[26]H.R. Rep. No. 1318, 74th Cong., 1st Sess. 29 (1935) (emphasis added).

[27]The Senate Report states that interstate distribution rates are left in the States' control. Obviously, the Senate drew a distinction between interstate distribution (left in the States' control) and interstate transmission (given to the FPC). Compare S. Rep. No. 621 at p. 49 with H.R. Rep. No. 1318 at p. 51.

The above legislative history on sections 201 and 206(b) does not provide any **[31,972]** definitive answers to the questions raised. We therefore turn to the case law under the FPA.

3. Case Law Under the FPA

Jersey Central was the first of the major FPC jurisdictional cases considered by the Supreme Court. The case involved the acquisition by New Jersey Power and Light Company (New Jersey Power) of certain securities of Jersey Central Power & Light Company (Jersey Central) without the Commission's prior approval. The question before the Court was whether Jersey Central was a "public utility" under section 201(e)[28] of the FPA so that the Commission's prior approval of the stock acquisition was necessary under section 203 of the FPA.

Jersey Central owned transmission facilities that connected to facilities that Public Service Electric & Gas Company (Public Service) owned. The interconnection of these transmission facilities was in New Jersey. Public Service's facilities in turn connected to the facilities of the Staten Island Edison Corporation (Staten Island Edison), a New York utility, at the mid-channel of Kill van Kull, a body

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[28]Section 201(e) defines a "public utility" as "any person who owns or operates facilities subject to the jurisdiction under this Part (other than facilities subject to such jurisdiction solely by reason of section 210, 211, or 212)." 16 U.S.C. §824(e). The section as adopted in 1935 did not contain the parenthetical, which was adopted in 1978 as part of the Public Utility Regulatory Policies Act.

of water separating New Jersey and New York. Jersey Central delivered energy to and received energy from Public Service under contract, and Public Service delivered energy to and received energy from Staten Island Edison under contract.[29]

The Court found that, although Jersey Central generated and received electricity only in New Jersey, some of the electric energy that it dispatched to Public Service "was instantaneously transmitted to New York."[30] The Court held that "[t]his evidence * * * furnishes substantial basis for the conclusion of the Commission that facilities of Jersey Central are utilized for the transmission of electric energy across state lines."[31] Therefore, the Court found that Jersey Central was a public utility within the meaning of section 201(e).[32]

The Court cited Attleboro, in which the Court found that the sale of locally produced electric energy for use in another state resulted in the transmission of electric energy in interstate commerce, even though title passed at the state line.[33] In Jersey Central, the Court explained the rationale for federal jurisdiction as follows:

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[29]Jersey Central, 319 U.S. at pp. 63-65.

[30]*Id.* at p. 66.

[31]*Id.* at p. 67 (citation omitted).

[32]*Id.* at p. 73.

[33]273 U.S. at pp. 86, 89-90.

(Section 201(c) of the FPA) defines the electric energy in commerce as that "transmitted from a State and consumed at any point outside thereof." There was no change in this definition in the various drafts of the bill. The definition was used to "lend precision to the scope of the bill." It is impossible for us to conclude that this definition means less than it says * * *. The purpose of this act was primarily to regulate the rates and charges of the interstate energy.[34]

The Court in Jersey Central thus interpreted the FPA as placing within the federal province regulation of wholesale sales of electric energy that, in any manner, flows in interstate commerce. The language quoted above and the citation to section 201(c) of the FPA, to be relied upon in subsequent Supreme Court cases, strongly suggested that the Commission's jurisdiction was not based on whether there was a sale by the utility, but rather on the flow of electric energy either into or out of a state, so long as the energy crosses state lines.

CL&P, which was decided two years after Jersey Central, is the leading case interpreting the section 201(b) local distribution proviso. In CL&P, the Commission sought to regulate the accounting practices of Connecticut Light & Power Company (CL&P).[35] At issue was whether **[31,973]** CL&P was a "public utility" under the FPA. The utility's system encompassed an area solely within a single state

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[34]319 U.S. at p. 71 (footnote omitted).

[35]CL&P, 324 U.S. at p. 517.

(Connecticut)[36] and did not interconnect with any other company that operated out of state.[37] "Its purchases and sales, its receipts and deliveries of power, [were] all within the state."[38] However, CL&P did purchase energy from companies that had, in turn, purchased energy from Massachusetts. The company also sold energy to a municipality that exported a portion of that energy to Fishers Island, located off the coast of Connecticut but "territory of New York."[39] The Commission based its jurisdiction on these few transactions.[40]

The Court of Appeals affirmed the Commission, holding that the Commission's jurisdiction extended to "electric distribution systems which normally would operate as interstate businesses." The Court of Appeals found that:

Whether or not the facilities by which petitioner distributes energy from Massachusetts should be classified as 'local' is not relevant to this case. The sole test of jurisdiction of the Commission over accounts is whether these facilities,

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[36] *Id.* at p. 518.

[37] *Id.* at p. 521.

[38] *Id.* at p. 522.

[39] *Id.* at pp. 519-21.

[40] *Id.*

'local' or otherwise, are used for the transmission of electric energy from a point in one state to a point in another.([41])

The Supreme Court reversed. It held that the statutory language in section 201(b) of the FPA providing that the Commission "shall not have jurisdiction * * * over facilities used in local distribution" is a limitation upon Commission jurisdiction that "the Commission must observe and the courts must enforce."[42] In analyzing the statute, the Court stated:

It has never been questioned that technologically generation, transmission, distribution and consumption are so fused and interdependent that the whole enterprise is within the reach of the commerce power of Congress, either on the basis that it is, or that it affects, interstate commerce, if at any point it crosses a state line.

* * * * *

But whatever reason or combination of reasons led Congress to put the provision in the Act, we think it meant what it said by the words "but shall not have jurisdiction * * * over facilities used in local distribution." Congress by these terms plainly was trying to reconcile the claims of federal and local authorities and to apportion federal and state jurisdiction over the industry.[43]

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[41] *Id.* at p. 522, *quoting Connecticut Light & Power Co. v. FPC*, 141 F.2d 14, 18 (D.C. Cir. 1944).

[42] 324 U.S. at p. 529.

[43] *Id.* at pp. 529-31.

The Court decided that this limitation on jurisdiction was "a legal standard that must be given effect in this case in addition to the technological transmission test."[44]

The Court stated that whether or not local distribution facilities carried out-of-state electric energy was irrelevant. Whatever the origin of the electric energy they carried, so long as the utility used the lines for local distribution,[45] they were exempt from federal jurisdiction.[46] In fact, the Court stated that local distribution facilities "may carry no energy except extra-state energy and still be exempt under the Act." Id. at 531. The Court concluded that the Commission's order:

> Must stand or fall on whether this company owned facilities that were used in transmission of interstate power and which were not facilities used in local distribution.[47]

Upon reversing the Court of Appeals, the Court commented, in dictum, on the evidence the Commission had relied upon in finding that the facilities in question were used for transmission. It noted that the Commission had relied upon certain gas transportation cases in concluding that transmission extends from the generator to the point where the

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[44]*Id.* at p. 531.

[45]It appears that while the Company received power (at one location) at 66 kV, it primarily owned facilities at 13.8 kV and below.

[46]324 U.S. at p. 531.

[47]*Id.* at p. 531 (emphasis added).

function of conveyance in bulk over distance is completed **[31,974]** and the process of subdividing the energy to serve ultimate consumers, which is the characteristic of "local distribution," is begun. The Court cautioned:

> But a holding that distributing gas at low pressure to consumers is a local business is not a holding that the process of reducing it from high to low pressure is not also part of such local business. In so far as the Commission found in these cases a rule of law which excluded from the business of local distribution the process of reducing energy from high to low voltage in subdividing it to serve ultimate consumers, the Commission has misread the decisions of this Court. No such rule of law has been laid down.[48]

The Court also noted in its dictum, however, that once a company is properly found to be a "public utility" under the Act, the fact that a local commission may also have jurisdiction does not preclude exercise of the Commission's functions. Id. at 533.[49] The Court instructed the lower court

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[48] *Id.* at p. 534.

[49] *See United States v. Public Utilities Commission of California*, 345 U.S. 295, 316 (1953) (Public Utilities Commission): Certainly the concrete fact of resale of some portion of the electricity transmitted from a state to a point outside thereof invokes federal jurisdiction at the outset, despite the fact that the power thus used traveled along its interstate route "commingled" with other power sold by the same seller and eventually directly consumed by the same purchaser-distributor.

See also Arkansas Power & Light Co. v. FPC, 368 F.2d

to remand the case to the Commission for a finding regarding whether the facilities in question were used in local distribution.[50]

The CL&P case was ultimately disposed of without the Commission having made a finding that the facilities were used in local distribution. While the Commission found that it was "extremely doubtful" that it could find that the facilities in question were not local distribution facilities, 6 FPC 104, 106 (1947), the Commission did not articulate a definition of local distribution facilities.

In Wisconsin-Michigan Power Co. v. Federal Power Commission,[51] the Seventh Circuit held that a utility was a jurisdictional public utility where it operated two divisions in Wisconsin and Michigan in a coordinated manner such that electric energy from one state was transmitted to the other, and vice versa, "in appreciable amounts by the power company and by it commingled with energy generated in the

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376, 383 (8th Cir. 1966) ("Where a company is in fact a public utility, all wholesale sales for resale in interstate commerce are subject to the provisions of sections 205 and 206 of the (FPA), regardless of the facilities used."). The Eighth Circuit further noted that the section 201(b) exemption applies to a company's status as a public utility and not to the Commission's jurisdiction over sales in interstate commerce for resale. *Id., citing Public Utilities Commission, Colton, infra, and Wisconsin-Michigan, infra.*

[50] *Id.* at p. 536.

[51] 197 F.2d 472 (7th Cir. 1952), cert. denied, 345 U.S. 934 (1953) (*Wisconsin-Michigan*).

two respective districts and then delivered to the [wholesale] customers * * *."[52] The court also rejected the notion that the energy changed its form or character when it was stepped down in voltage before it reached the wholesale purchasers.[53]

The court in Wisconsin-Michigan distinguished between transmission and local distribution by focusing on wholesale sales of electric energy versus retail sales ("local rates") of electric energy. It cited the House Report on the FPA, and characterized the legislative history as follows:

The legislative history, (H.R. Rep. No. 1318), 74th Cong., 1st Sess. pages 7, 8 and 27 (1935), discloses that the Congressional Committee intended that the provisions of the (FPA) should apply to the transmission of electric energy in interstate commerce, i.e., the sale of energy at wholesale in interstate commerce, but not to the retail sale of any such energy in local distribution; that the (FPA) left to the state the authority to fix local rates where the energy is brought in from other states, and that the rate making power of the [FPC] was to be confined to those wholesale transmissions which the Supreme Court had held in (Attleboro) to be beyond the reach of the state. Under that decision, said the committee, the rates **[31,975]** charged in interstate wholesale transactions could not

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[52] *Id.* at p. 474.

[53] *Id.* ("Obviously the energy thus transmitted in interstate commerce is not changed in form or in character except that the voltage is reduced to an extent consistent with efficient economic management and operation.").

be regulated by the states. It defined a wholesale transaction as the sale of electric energy for resale.[54]

The Seventh Circuit's characterization of the House Report seems to equate transmission of electric energy in interstate commerce with the sale of energy at wholesale in interstate commerce. However, this interpretation is at odds with both the plain words of the statute as well as the language of the House Report, both of which refer to transmission in interstate commerce separately from sales for resale in interstate commerce.[55] In addition, the Senate Report, which the Seventh Circuit did not mention, clearly recognized jurisdiction over all interstate transmission lines, whether or not a sale of energy is carried by those lines.[56]

The Wisconsin-Michigan court also cited analogous natural gas cases, stating that "[t]he question is essentially, when does interstate commerce transportation end and where

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[54]197 F.2d at p. 476 (emphasis added).

[55]See H.R. Rep. No. 1318 at p. 27. ("Subsection (b) confers jurisdiction upon the Commission over the transmission of electric energy in interstate commerce and the sale of electric energy in wholesale in interstate commerce * * *." emphasis added).

[56]See S. Rep. No. 621 at p. 48 ("Jurisdiction is asserted over all interstate transmission lines whether or not there is a sale of the energy carried by those lines * * *.").

do the local distribution facilities first become operative."[57] The court further stated that:

(U)pon delivery to (the wholesaler) local distribution begins when he resells. His sales and distribution at retail are clearly local in character, and constitute only local distribution; but at no point before delivery to him has been completed, has interstate transmission terminated. In other words, "facilities used in local distribution" means facilities used for making resale and distribution to consumers, jurisdiction over which is left to the states. It was only because of this conclusion that the Supreme Court said, [citation omitted], the Act "cut[s] sharply and cleanly between sales for resale and direct sales for consumptive uses." We think there is no ground for the position that local distribution includes any transmission occurring before the wholesaler who resells at retail is reached.[58]

The Seventh Circuit concluded that the sales for resale were made in interstate commerce; that local distribution had not begun; that the interstate character of the transmission persisted until delivery to the wholesaler; that, up to that point, no local distribution facilities were in operation and that, therefore, the sales were subject to Commission regulation.

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[57] 197 F.2d at p. 477.

[58] *Id.*, citing *FPC v. East Ohio Gas Co.*, 338 U.S. 464 (1950) (East Ohio).

In Federal Power Commission v. Southern California Edison Company (the Colton case),[59] the Supreme Court held that the FPA provides a clear line of demarcation between jurisdictional transactions and non-jurisdictional transactions. However, this case, too, involved bundled sales of electric energy. In the facts of the case, Southern California Edison Company (Edison) admitted that it was a public utility by virtue of owning two interstate transmission lines.[60] At issue was whether its sales of electric energy to the City of Colton, California, for resale to Colton's retail customers, were jurisdictional. Included in the electric energy that Edison sold to Colton was out-of-state electric energy from Hoover Dam.[61] The Commission ruled that the sale to Colton was a sale of electric energy at wholesale in interstate commerce subject to regulation under the FPA.[62] In upholding the Commission, the Court held that Edison's importation of out-

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[59]376 U.S. 205 (1964) (Colton).

[60]The Supreme Court noted that Edison's status as a public utility did not decide the question of whether the FPC could assert jurisdiction over the rates for the Edison-Colton sale. Id. at p. 208 n.3.

[61]*Id.* at p. 208, 209 & n.5.

[62]*Id.* at p. 208. *See Arkansas Electric Cooperative Corp. v. Arkansas Public Service Commission*, 461 U.S. 375, 380 (1983) ("(Colton) held, among other things, that * * * a California utility that received some of its power from out-of-state was subject to federal and not state regulation in its sales of electricity to a California municipality that resold the bulk of the power to others.").

of-state electricity for resale to Colton sufficed to confer federal jurisdiction.

[31,976]

The Court, citing an earlier Supreme Court case,[63] characterized Congressional intent in the FPA:

(W)hat Congress did was to adopt the test developed in the Attleboro line which denied state power to regulate a sale "at wholesale to local distributing companies" and allowed state regulation of a sale at "local retail rates to ultimate consumers."[64]

The Court rejected the argument that FPC jurisdiction was confined to those interstate wholesale sales constitutionally beyond the power of state regulation by force of the Commerce Clause, and was to be determined on a case-by-case analysis of the impact of state regulation upon the national interest. The Court stated that in the FPA:

(C)ongress meant to draw a bright-line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis. This was done in the Power Act by making FPC jurisdiction plenary and extend[ed] it to all wholesale sales in interstate commerce except those

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[63] *Illinois Natural Gas Co. v. Central Illinois Public Service Co.*, 314 U.S. 498, 504 (1942).

[64] 376 U.S. at p. 214.

which Congress has made explicitly subject to regulation by the States.[65]

The Court held that "[t]here is no such exception covering the Edison-Colton sale."[66]

Parties in the Colton case had raised the question of whether jurisdiction over the Colton sale was prevented by the "local distribution" proviso of section 201(b). The Court stated that whether facilities are local distribution facilities is a matter for the Commission to decide in the first instance. Citing CL&P, supra, it stated:

Whether facilities are used in local distribution -- although a limitation on FPC jurisdiction and a legal standard that must be given effect in addition to the technological transmission test * * * -- involves a question of fact to be decided by the FPC as an original matter.[67]

The Court cited evidentiary support and the Commission's expertise in such matters in upholding the Commission's determination that certain facilities owned by Edison were used exclusively to effect the wholesale sale to Colton and not for local distribution. Such facilities included 12 kV lines that served an industrial customer, several lighted highway signs, a residence and a railroad section house before they reached the transformers in the Colton substation. The

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[65] *Id.* at pp. 215-216.

[66] *Id.* at p. 216 (footnote omitted).

[67] *Id.* at p. 210 n.6 (citation omitted).

FPC had held that those uses prior to the lines reaching the Colton substation did not transform the lines into local distribution facilities.[68]

In Duke Power Company v. Federal Power Commission (Duke),[69] the D.C. Circuit held that a public utility's acquisition of facilities used solely in local distribution, and which would continue to be used for local distribution, was beyond the Commission's jurisdiction under section 203. The case involved Duke Power Company's (Duke's) proposed acquisition of facilities owned by Clemson University (Clemson), which were used to distribute electricity off-campus to customers (primarily university personnel) in two South Carolina counties. Clemson purchased the power at wholesale from Duke. No one appeared to contest the conclusion that the 7 miles of distribution line and 418 service connections owned by Clemson were "local distribution" facilities.[70] Rather, the case turned on interpreting section 203 and whether it was intended to affect only acquisitions of jurisdictional facilities, or also to affect acquisitions of non-jurisdictional facilities. In interpreting section 203, however, the D.C. Circuit extensively analyzed and discussed the fundamental jurisdictional lines that Congress drew in section 201.

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[68] *Id.* at p. 210 n.6.

[69] 401 F.2d 930 (D.C. Cir. 1968) (Duke).

[70] Duke delivered power to Clemson at a distribution voltage of 4,160 volts. The step-down transformers by which the voltage was reduced, and the substations at which the delivery was effected, were owned by Duke. 401 F.2d at p. 931, n.8.

Citing to the CL&P case, the court in Duke stated:

The Act, as we have seen, effectuated federal control over the transmission and the sale at wholesale of electric energy in **[31,977]** interstate commerce, and established the Commission's regulatory power over public utilities engaging in either of these pursuits.[71]

However, quoting CL&P, the court further stated:

The expression "facilities used in local distribution" is one of relative generality. But as used in this Act it is not a meaningless generality in the light of our history and the structure of our government. We hold the phrase to be a limitation on jurisdiction and a legal standard that must be given effect in this case in addition to the technological transmission test.[72]

The court further rejected the Commission's concept that, in order to determine whether jurisdiction over any particular acquisition existed, the impact of local supervision be measured on a case-by-case basis. Quoting from Colton, the court stated:

[T]his "flexible approach" -- involving as it does the consideration, inter alia, of "the effect of the regulation upon the national interest in the commerce" -- has been flatly rejected as a technique for resolving jurisdictional conflicts

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[71]401 F.2d at pp. 938-39 (emphasis added, footnotes omitted).

[72]*Id.* (footnote omitted).

between the Commission and state bodies * * * We think that like the line "(i)t cut sharply and cleanly between sales for resale and direct sales for consumptive uses" to facilitate jurisdictional determinations in rate regulation, "Congress meant to draw a bright line easily ascertained, between state and federal jurisdiction, making unnecessary such case-by-case analysis," in distributing regulatory power over the acquisition of facilities.[73]

The court rejected the Commission's argument that jurisdiction over the merger or consolidation of jurisdictional facilities with those of any other "person" under section 203 gave the Commission jurisdiction over Duke's acquisition. The court stated that the FPA reflects a policy "'that matters largely of a local nature, even though interstate in character, should be handled locally and should receive the consideration of local [officials] familiar with the local conditions in the communities involved.'"[74]

Federal Power Commission v. Florida Power & Light Company[75] is the last major court case to address the Commission's transmission jurisdiction. In this case, the Commission sought to impose its accounting rules upon

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[73]*Id.* at p. 949 (footnotes omitted).

[74]*Id.* at p. 936 (quoting from Hearings on H.R. 5423 before the House Committee on Interstate and Foreign Commerce, 74th Cong., 1st Sess. 393 (1935) (testimony of then-FPC Commissioner Seavey)).

[75]404 U.S. 453, *reh'g denied*, 405 U.S. 948 (1972) (*Florida Power & Light*).

Florida Power & Light Company (Florida Power & Light). The company's system lay solely within the borders of Florida and did not directly connect with any out- of-state utility.[76] The Commission held that Florida Power & Light did own facilities that transmitted electric energy in interstate commerce, but the Court of Appeals for the Fifth Circuit ruled that the Commission did not have substantial evidence to support its finding.

The Supreme Court reversed. The Supreme Court noted that Florida Power & Light was a member of the Florida Power Pool along with Florida Power Corporation (Florida Power Corp.).[77] In turn, Florida Power Corp. connected with Georgia Power Company (Georgia Power) at a "bus"[78] south of the Georgia-Florida border.[79] Florida Power Corp. regularly exchanged power with Georgia Power.[80] In many instances, Florida Power Corp. transferred power to Florida Power & Light instantly after receiving power from Georgia Power, and transferred power to Georgia Power immediately after receiving power from Florida Power

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[76]404 U.S. at p. 456.

[77]*Id.* at p. 456.

[78]A "bus" is a connector or group of connectors that serves as a common connection for two or more circuits.

[79]404 U.S. at p. 457.

[80]*Id.*

& Light.[81] The Supreme Court found that power commingled in the bus moved across state lines, and concluded that Florida Power & Light engaged in transmission in interstate commerce. The **[31,978]** Court held that, to establish jurisdiction, the Commission need only show that "some [Florida Power & Light] power goes out of State."[82] The Court further explained that "(i)f any (Florida Power & Light) power has reached Georgia, or (if Florida Power & Light) makes use of any Georgia power * * * FPC jurisdiction will attach * * *."[83]

There is also a line of cases that address, among other things, what constitutes a Commission jurisdictional "sale of electric energy at wholesale"[84] under section 201 of the FPA.[85] These cases all concerned bundled sales. While the issues posed above involve unbundled wheeling, the "resale" cases are helpful to the extent they suggest that local distribution takes place only after power is subdivided. See, e.g., 345 U.S. at 316 ("the facilities supplied 'local

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[81] *Id.* at p. 457 & n.8.

[82] *Id.* at p. 461. (emphasis omitted).

[83] *Id.* at p. 461 n.10. (emphasis added).

[84] See Section 201(d), 16 U.S.C. §824(d) (1988).

[85] *Public Utilities Commission*, supra note 345; *City of Oakland, California v. FERC*, 754 F.2d 1378 (9th Cir. 1985) (*Oakland*). *See also Alexander v. FERC*, 609 F.2d 543 (D.C. Cir. 1979) (*Alexander*).

distribution' only after the current was subdivided for individual consumers.").

4. Natural Gas Act

The Natural Gas Act (NGA) was adopted in 1938. Like the FPA, the NGA contains language limiting the Commission's jurisdiction in situations involving local distribution.[86]

Section 1(b) of the NGA provides:

The provisions of this Act shall apply to the transportation of natural gas in interstate commerce, to the sale in interstate commerce of natural gas for resale for ultimate public consumption for domestic, commercial, industrial, or any other use, and to natural gas companies engaged in such transportation or sale, but shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural.[87]

There is similarity in many respects between the House and Senate Reports on the FPA and the NGA with respect to the jurisdiction given the Commission. For example, all four reports mention Attleboro as placing interstate wholesale transactions beyond the reach of the

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[86]Courts often rely on cases construing the NGA when interpreting the FPA, and vice versa. *E.g., Arkansas Louisiana Gas Co. v. Hall*, 453 U.S. 571, 577 n.7 (1981).

[87]15 U.S.C. §717(b) (emphasis added).

States. As indicated in the House Report on the NGA, the States could "regulate sales to consumers even though such sales are in interstate commerce, such sales being considered local in character and in the absence of congressional prohibition subject to State regulation." (See H.R. Rep. No. 709, 75th Cong., 1st Sess. 1). However, the House and Senate Reports on the NGA contain identical language not found in the reports on the FPA:

In view of the importance of section 1(b), which states the scope of the act, it seems advisable to comment on certain provisions appearing therein. It will be noted that this subsection of the bill, after affirmatively stating the matters to which the act is to apply, contains a provision specifying what the act is not to apply to, as follows:

But shall not apply to any other transportation or sale of natural gas or to the local distribution of natural gas or to the facilities used for such distribution or to the production or gathering of natural gas.

The quoted words are not actually necessary, as the matters specified therein could not be said fairly to be covered by the language affirmatively stating the jurisdiction of the Commission, but similar language was in previous bills, and, rather than invite the contention, however unfounded, that the elimination of the negative language would broaden the scope of the act, the committee has included it in this bill. That part of the negative declaration stating that the act shall not apply to "the local distribution of natural gas" is surplusage by reason of the fact that distribution is made only to consumers in connection with sales, and since no jurisdiction is given to the Commission to regulate sales to consumers the

Commission would have no authority over **[31,979]** distribution, whether or not local in character. (Emphasis added).[88]

As a result of this language it can be argued that Congress considered distribution (and local distribution) only in the context of bundled retail sales of natural gas. In fact, it appears that all of the court cases affirming the states' right to regulate local distribution of gas have involved bundled retail sales. See Panhandle Eastern Pipe Line Co. v. Michigan Public Service Commission, 341 U.S. 329 (1951) (Panhandle). There the Court, in affirming the State of Michigan's right to regulate an interstate pipeline's proposed bundled retail sales of gas to industrial consumers, noted that the pipeline company proposed to lay pipeline in "the streets and alleys of Detroit" and ignored the local distribution company's request for additional gas to meet the increased needs of the industrial consumers. Id. at 333. While the Court based its holding on a state's authority to regulate direct (retail) sales to an end- user, rather than on the basis of the section 1(b) local distribution provision, it also found that the proposed sales were "primarily of local interest" and "emphasized the need for local regulation." Id. Two years before Panhandle, the Supreme Court issued its decision in FPC v. East Ohio Gas Co., 338 U.S. 465 (1949) (East Ohio). East Ohio Gas Company owned and operated a natural gas business wholly within the State of Ohio. The company sold gas only to Ohio customers but most of the gas was transported to Ohio from other states by interstate pipelines.

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[88]H.R. Rep. No. 709, 75th Cong., 1st Sess. 3 (1937); S. Rep. No. 1162, 75th Cong., 1st Sess. 3 (1937).

These interstate pipelines connected inside Ohio with East Ohio's large high pressure lines. The gas then was transported over 100 miles through East Ohio's system to its local distribution system. East Ohio argued that it was exempt from Commission jurisdiction because all of its facilities were local distribution. The Court disagreed, finding the Commission's jurisdiction extends over the transportation of gas in interstate commerce through high-pressure transmission lines and that distribution did not begin until the point where pressure is reduced and gas enters local mains. The Court stated that: "[w]hat Congress must have meant by 'facilities' for 'local distribution' was equipment for distributing gas among customers within a particular local community, not the high-pressure pipelines transporting the gas to the local mains."[89]

The Commission relied in part on East Ohio's high pressure/low pressure distinction in a recent NGA section 7 certificate case which authorized construction of facilities to bypass the local distribution company.[90] On appeal, the California Commission argued that under section 1(b) it should at least have "jurisdiction over the 'taps, meters and

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[89]338 U.S. at pp. 469-70.

[90]*See Mojave Pipeline Company*, 35 FERC ¶61,199 (1986), *reh'g denied*, 41 FERC ¶61,040 (1987), *reh'g denied*, 42 FERC ¶61,351 (1988); *see also Mojave Pipeline Company*, 66 FERC ¶61,194 (1994), *reh'g pending*.

other tie-in facilities' that link the pipeline to end users."[91] The court disagreed:

> While as a matter of ordinary English 'local distribution' might be understood to encompass any delivery to an end user, that is hardly the only or even more plausible reading. Distribution conjures up receiving a large quantity of some good and parcelling it out among many takers.[92]

After reviewing the report language discussed above, the court also stated:

> Insofar as congressional committees spoke to the matter * * * they appear to have viewed distribution as confined to its parcelling out function and (probably) even more narrowly, to parcelling out accompanied by retail sales.[93]

In Cascade Natural Gas Corporation v. FERC, et al. (Cascade), the court affirmed the Commission's authorizing an interstate pipeline under section 7 of the NGA "to construct a tap and meter facility that would allow it to deliver natural gas directly to two industrial consumers **[31,980]**

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[91] *See Public Utilities Commission of the State of California v. FERC, et al.*, 900 F.2d 269, 273 (D.C. Cir. 1990) (footnote omitted) (*WyCal*).

[92] *Id.* at p. 276.

[93] *Id.* (emphasis in original).

* * *."[94] To reach the interstate pipeline, the industrials constructed a nine-mile pipeline. Together, the facilities bypassed the local distribution company.[95]

The court rejected arguments that section 1(b) deprived the Commission of jurisdiction holding that:

"Local distribution," as Congress viewed the term, involves two components: the retail sale of natural gas and its local delivery, normally through a network of branch lines designed to supply local consumers.[96]

5. Analysis

a. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier to a purchaser who will then re-sell the energy to an end user?

The case law supports the conclusion that any facilities of a public utility used to deliver electric energy in interstate commerce to a wholesale purchaser, whether such facilities are labeled "transmission," "distribution" or "local

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[94]955 F.2d 1412, 1414 (10th Cir. 1992).

[95]Unlike the situation in WyCal where the pipeline made direct sales to end users, in Cascade the pipeline transported gas purchased from third parties. *See Northwest Pipeline Corporation*, 51 FERC ¶61,289 at p. 61,909 (1990).

[96]Cascade, 955 F.2d at p. 1421.

distribution," are subject to the Commission's jurisdiction under sections 205 and 206.

This conclusion is supported by Public Utilities Commission, supra, in which the Supreme Court, in the section of its opinion addressing the section 201(b) local distribution provision, held that local distribution facilities began "only after the current was subdivided for individual consumers."[97] Wisconsin-Michigan, supra, in which the Seventh Circuit held that there is no local distribution until the wholesaler who re-sells at retail is reached, is to like effect.

This conclusion, which results in a "functional" line being drawn to determine Commission jurisdiction, is not only consistent with the case law under section 201, but is also consistent with our interpretation of the line drawn under newly amended FPA sections 211 and 212. As long as electric energy is being sold to a legitimate wholesale purchaser, we believe the Commission has jurisdiction under sections 201, 205, and 206 of the FPA over the public utility's facilities used to deliver electric energy to that purchaser.

b. What facilities are jurisdictional to the Commission in a situation involving the unbundled delivery in interstate commerce by a public utility of electric energy from a third-party supplier directly to an end user?

In analyzing jurisdiction over unbundled retail wheeling, we believe it is important to distinguish between unbundled wheeling provided by the public utility who

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[97]345 U.S. at p. 316 (footnote omitted).

previously provided bundled retail service to the end user, and unbundled wheeling provided by other public utilities to the end user. For example, a former bundled retail customer may need unbundled wheeling services from its previous public utility generation supplier, as well as unbundled wheeling from one or more intervening public utilities, in order to reach a distant generation supplier. In this scenario, the Commission believes it would have jurisdiction over all of the facilities used for the unbundled wheeling provided by the intervening public utilities.[98] The more difficult issue is whether some portion of the facilities used to transmit energy from the transmitting utility in closest proximity to the end user (the former supplier of the bundled product) is local distribution facilities. We believe that in most, if not all circumstances, some portion will be local distribution facilities.

The case law is replete with statements that the local distribution provision of section 201 must be given effect. However, the Supreme Court in both CL&P and Colton, supra, has stated that whether facilities are used in local distribution is a question of fact to be decided by the Commission as an original matter. Thus, there is no clear case law on a "bright line" between transmission and local distribution. In addition, regardless **[31,981]** of the details of the chain of delivery services necessary to move electric energy from the generator to the end user, in most cases the last public utility in the chain will use facilities that

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[98]The Commission would not have jurisdiction over the rates for the sale of generation by the distant supplier because the transaction would be a retail sale of electric energy.

historically were considered local distribution facilities. Accordingly, unlike the situation involving unbundled wholesale wheeling, for which the case law clearly supports a "functional" test, the Commission believes the case law and practical realities of a changing industry support an analysis of local distribution facilities based on the facilities' functional as well as technical characteristics.

While it would be preferable to draw an absolutely "bright" line (e.g., based on technical characteristics such as voltage), the Commission does not believe this is required by the case law and, importantly, would not be a workable approach in all cases because of the variety of circumstances that may arise and because utilities themselves classify facilities differently (e.g., one utility may classify a 69 kV facility as transmission; another may classify it as distribution).

Therefore, the Commission is adopting several indicators it will evaluate in determining whether particular facilities are transmission or local distribution in the case of vertically integrated transmission and distribution utilities:[99]

•Local distribution facilities are normally in close proximity to retail customers.

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[99]In the case of a distribution-only utility, which is franchised by a State or local government and sells only at retail, all of the circuits (and related wires, transformers, towers, and rights of way) which it owns or operates (regardless of voltage) would be local distribution facilities.

•Local distribution facilities are primarily radial in character.

•Power flows into local distribution systems, it rarely, if ever, flows out.

•When power enters a local distribution system, it is not reconsigned or transported on to some other market.

•Power entering a local distribution system is consumed in a comparatively restricted geographical area.

•Meters are based at the transmission/local distribution interface to measure flows into the local distribution system.

•Local distribution systems will be of reduced voltage.[100]

In summary, for unbundled wholesale wheeling the Commission will apply a functional test. The only definitive question will be whether the entity to whom the power is delivered is a lawful wholesaler. For unbundled retail wheeling the Commission will apply a combination functional-technical test that will take into account technical characteristics of the facilities used for the wheeling. The

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[100]The Commission has analyzed utilities' filings required by the Commission's regulations. These filings are made on FERC Form No. 1. While there is no uniform breakpoint between transmission and distribution, it appears that utilities account for facilities operated at greater than 30 kV as transmission and that distribution facilities are usually less than 40 kV.

Commission concludes that these tests are consistent with the FPA, its legislative history and the case law discussed above.

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